

BEFORE  
THE PUBLIC SERVICE COMMISSION  
OF SOUTH CAROLINA  
Docket No. 2019-290-WS – Order No. 2020-\_\_\_\_

April 9, 2020

In Re:

Application of Blue Granite Water  
Company for Approval to Adjust Rate  
Schedules and Increase Rates

---

)  
)  
)  
)  
)  
)

*proposed*  
ORDER

TABLE OF CONTENTS

I. Executive Summary .....	3
II. Introduction .....	6
III. Overview of Company’s Requested Relief .....	10
IV. Statutory Standards and Required Findings .....	12
V. Review of the Evidence and Evidentiary Conclusions .....	15
A. Areas of Agreement and Compromise .....	15
B. Areas of Dispute .....	17
i. Cost of Capital .....	17
ii. Depreciation Rates .....	32
iii. Non-Revenue Water .....	43
iv. Pass-Through Mechanism for Purchased Services .....	46
v. Deferred Maintenance Expenses .....	53
vi. Amortization of Deferral Balances .....	55
vii. Accumulated Depreciation and Accumulated Amortization of CIAC .....	60
viii. Storm Recovery Expense .....	63
ix. Storm Reserve Fund .....	65
x. Round Up Program and Associated Costs .....	67
xi. Rate Case Expense and Other Legal Expenses .....	70
xii. Rent Expense .....	73
xiii. Insurance Expense .....	75
xiv. Administrative Office Upfit Costs .....	76
xv. Employee Service Award Costs .....	80
xvi. LETTS Tank Pumping Charges .....	82
xvii. Cost of Service and Tariff Rate Design .....	85
xviii. Other Issues .....	89
xix. Use of Charlotte Interconnection .....	94
VI. Findings of Fact and Conclusions of Law .....	96
VII. Ordering Paragraphs .....	100

## I. EXECUTIVE SUMMARY

In the interest of transparency, and to provide a condensed explanation of our reasoning with respect to certain significant components of this Order, we offer the following Executive Summary of issues.

### **Rate Increase Generally**

The rate increase in this case is, in some ways, the product of a perfect storm. The evidence in the record supports the conclusion that water and wastewater infrastructure in this state is aging and nearing the end of its life. There is also evidence in the record that supports the conclusion that the rates of Blue Granite have been artificially low for some time. The Company has hired new management and operations personnel, and the Company is now, in good faith, prioritizing necessary investments in its systems. At the same time, the Company's third-party providers have faced similar challenges and are needing to increase their own rates. The net effect of these factors is a rate increase for customers that is necessary to support the systems on which they continually rely for reliable delivery of clean water and responsible treatment of wastewater.

While a rate increase is unavoidable in light of these issues, the Company has proposed—and we approve, as discussed below—certain rate features that will assist and benefit customers in the long-term. Among these are (1) the pass-through mechanism, which will mitigate the rate shock that would otherwise occur in the Company's next rate case resulting from accumulated increases in third-party expenses and prevent the incurrence of carrying costs on deferred amounts; (2) the Round Up program, which will assist customers in need with their water and wastewater utility bills; and (3) a Storm Reserve Fund, which will enable Blue Granite to promptly respond to

catastrophic storm events without the need to pass on to customers carrying costs on deferred expenses.

In light of the evidence received in this case, the testimony provided in response to questions from counsel and from this Commission, and the collective efforts of the parties and this Commission to scrutinize the application and its supporting documents, we are confident that the rate increase in this case is limited to only that which is lawfully authorized and necessary for the reliable provision of utility service.

#### **Return on Equity**

As discussed below, we approve an overall cost of capital for Blue Granite of 8.12%, based on the Company's actual capital structure at June 30, 2019 (52.91% equity and 47.09% debt), the Company's actual cost of long-term debt (5.73%), and a cost of equity of 10.25%. Such an authorized cost of capital should be adequate to provide Blue Granite with the opportunity to earn a return on equity that is: (1) adequate to attract capital at reasonable terms; (2) sufficient to ensure its financial integrity; and (3) commensurate with returns on investments in enterprises having corresponding risks. This, in turn, should enable Blue Granite to provide safe, reliable utility service while maintaining its financial integrity, all to the benefit of both investors and customers.

#### **Non-Revenue Water & Water Audit**

As discussed below, for some systems, the cost of leak testing would exceed—and, in some cases, greatly exceed—the cost of non-revenue water. These are costs for which customers would be responsible. For that reason, disallowing Blue Granite's recovery of non-revenue water in cases where it is not economical to invest would incentivize the Company to make uneconomic investments, which would actually drive up costs for customers rather than insulate them. We find

below that it would be unreasonable for this Commission to require customers to pay large sums for leak detection in cases where the related costs would exceed the non-revenue water costs. For that reason, for the four systems for which leak detection would actually be economical, we direct that the Company begin leak testing and associated repairs within 12 months of this order. We also disallow recovery of purchased water expenses for these four systems above the 20 percent non-revenue water level, and direct the Company to contract with a third party for the purpose of conducting a water audit for its purchased water systems.

### **Pass-Through Mechanism**

As discussed below, we approve the pass-through mechanism as modified in this order. While we find that the pass-through mechanism benefits customers by annually adjusting rates based on periodic changes in third-party service providers' rates, we agree with ORS that the Company should be provided incentive to reduce non-revenue water. We therefore direct Blue Granite to exclude from its annual pass-through recovery all non-revenue water above 20 percent of its purchased water expenses for the four systems for which leak testing would be economical. We believe that this modification to the mechanism appropriately updates third party rate changes, but also provides incentive to the Company to make the investments and improvements necessary to reduce non-revenue water.

### **Administrative Office Upfit Costs**

As discussed below, we find that the Company's headquarters office upfit costs should be reflected in rates approved in this proceeding. The evidence demonstrates that the Company made a reasonable business decision to relocate its headquarters office, and that the costs it incurred in upfitting its Greenville office were necessary and reasonable.

## II. INTRODUCTION

This matter comes before the Public Service Commission of South Carolina (the “Commission”) by way of Blue Granite Water Company’s (“Blue Granite” or the “Company”) Application for Approval to Adjust Rate Schedules and Increase Rates (“Application”) pursuant to S.C. Code Ann. § 58-5-240 and S.C. Code Ann. Regs. 103-823.

On August 30, 2019 the Company filed its Notice of Intent to File Application, and on October 2, 2019 its Application was filed with the Commission. On October 23, 2019, the Commission Clerk’s Office issued the Notice of Filing and Hearing and Prefile Testimony Deadlines (Notice for Newspapers) and Notice of Filing and Hearing and Prefile Testimony Deadlines (Notice for Customers) and instructed the Company to publish the Notice for Newspapers in newspapers of general circulation in the areas affected and to furnish the Notice for Customers by U.S. Mail, via bill inserts or by electronic mail to each affected customer by November 25, 2019. Proof of Publication of the Notice for Newspapers and Certification of the Notice for Customers was to be filed with the Commission on or before December 16, 2019. The Company filed a letter requesting additional time to complete the notification to customers. On October 24, 2019, the Commission Clerk’s Office issued a Revised Notices of Filing and Hearing and Prefile Deadlines (Notice to Customers) and a Revised Notice of Filing and Hearing and Prefile Deadlines (Notice to Newspapers). On December 3, 2019, the Company filed with the Commission Proofs of Publication from The State, The Post and Courier, The Greenville News, The Herald Fort Mill Times and The Greenwood Index-Journal; Affidavit of Mailing to all water distribution and sewer customers; and Certification of Mailing to the County and City

Administrators demonstrating that the Revised Notice of Filing and Hearing and Prefile Testimony Deadlines was duly published in accordance with the Docketing Department's instructions.

Pursuant to Commission Order Nos. 2019-804, 2019-830, 2019-831, 2019-825, 2019-827, and 2019-829, the Docket Department issued a Notice of Public Night Hearings to be held in the Town of Irmo, and the Counties of Anderson, Greenville, Lexington, Richland, Union and York. The Company was instructed to furnish the Notice of Public Night Hearings by January 14, 2020, to each affected customer. On January 16, 2020, the Company filed its Affidavit of Mailing of the Notice of Public Night Hearings to each affected customer.

The Office of Regulatory Staff ("ORS"), automatically a party pursuant to S.C. Code Ann. § 58-4-10(B), was represented by Andrew M. Bateman, Esquire, Alexander W. Knowles, Esquire and Christopher Huber, Esquire. Forty Love Point Homeowners' Association ("Forty Love"), represented by Laura Valtorta, Esquire, filed a petition to intervene on October 15, 2019. The Building Industry Association of South Carolina ("BIA") represented by John J. Pringle, Jr., Esquire, filed a petition to intervene on November 5, 2019. The South Carolina Department of Consumer Affairs ("Consumer Affairs"), represented by Carri Grube Lybarker, Esquire, Becky L. Dover, Esquire, Roger P. Hall, Esquire, and Richard L. Whitt, Esquire, filed a petition to intervene on November 25, 2019. On December 11, 2019, the Town of Irmo represented by S. Jahue Moore, Esquire, filed a petition to intervene. Jim Knowlton, self-represented, filed a petition to intervene on December 16, 2019. SteFan Dover, self-represented, filed a Petition to Intervene on December 17, 2019. York County, South Carolina ("York County"), represented by Michael K. Kendree, Esquire, filed a petition to Intervene on December 17, 2019. Blue Granite was represented by Frank R. Ellerbe, III, Esquire, and Samuel J. Wellborn, Esquire. Collectively, Blue Granite, ORS,

Forty Love, BIA, Consumer Affairs, the Town of Irmo, Jim Knowlton, SteFan Dover, and York County are referred to as the “Parties” or individually as a “Party.”

On December 30, 2019, the Company filed the direct testimony of Dylan D’Ascendis, Donald Denton, Dante DeStefano, Shawn Elicegui, Bryce Mendenhall, and John Spanos. Exhibits were included in the direct testimony of Dylan D’Ascendis, Dante DeStefano, Shawn Elicegui, and John Spanos. The corrected direct testimony and exhibit of Dylan D’Ascendis was filed on January 10, 2020.

On January 21, 2020, Forty Love filed the direct testimony of its witness, Reid Radtke and on January 23, 2020 filed the direct testimony of its witness Barbara King. On January 23, 2020, the Consumer Affairs filed the direct testimony and exhibits of its witnesses, Lafayette K. Morgan, Jerome D. Mierzwa, and Aaron L. Rothschild. The ORS filed direct testimony on January 23, 2020, of its witnesses David C. Parcell, Charles E. Jackson, Brandon S. Bickley, Anthony M. Sandonato, Anthony D. Briseno, Kyle D. Maurer, Sr., David J. Garrett, and Daniel F. Sullivan. Exhibits were included with the direct testimony of witnesses Parcell, Bickley, Sandonato, Briseno, Maurer, Garrett and Sullivan. York County on January 23, 2020, filed the direct testimony of its witness Erick Rekitt. Jim Knowlton’s direct testimony was filed on January 23, 2020. The direct testimony of SteFan Dover was filed on January 23, 2020.

On January 31, 2020 Consumer Affairs filed corrected direct testimony of witnesses Morgan and Rothschild and filed corrected exhibits on February 2, 2020. Updated corrected Exhibits of Rothschild were filed on February 28, 2020.



On February 6, 2020, the Company filed Rebuttal Testimony of Dylan D’Ascendis, Donald Denton, Dante DeStefano, Bryce Mendenhall and John Spanos. Exhibits were included in the Rebuttal Testimony of Dylan D’Ascendis, Dante DeStefano, and Bryce Mendenhall.

On February 14, 2020, the Consumer Advocate filed surrebuttal testimony of witnesses Mierzwa, Rothschild, and Morgan. The ORS filed the surrebuttal testimony of witnesses Bickley, Briseno, Garrett, Jackson, Maurer, Parcell, Sandonato and Sullivan on February 14, 2020, and on February 24, 2020, filed revised surrebuttal testimony of witnesses Briseno, Sandonato, Sullivan, and Maurer.

Public Hearings were held on January 27, 2020 in Lexington, SC; January 30, 2020 in Irmo, SC; February 3, 2020 in Union, SC; February 13, 2020, in Greenville; February 27, 2020 in Columbia, SC and March 5, 2020, in York, SC.

In Order No. 2020-150, issued on February 19, 2020, the Commission granted the Company’s Motion to Permit Witness Appearance by Videoconference as Related to the Presentation of Testimony of Shawn EliceGUI. On February 24, 2020, the Standing Hearing Officer granted the request of the Consumer Affairs to present the testimony of its witness Jerome D. Mierzwa by Videoconference. Mierzwa’s testimony was scheduled with the two other live witnesses on behalf of the Consumer Affairs in a three-person panel and scheduled to testify on Thursday, February 27, 2020.

The Commission conducted an evidentiary hearing on this matter from February 26, 2020 through March 2, 2020 in the hearing room of the Commission with Honorable Comer H. Randall presiding.

Each referenced witness appeared, gave summaries of his or her testimony, and answered questions from counsel and the Commission.

### **III. OVERVIEW OF COMPANY'S REQUESTED RELIEF**

Blue Granite seeks to increase its water and wastewater rates to recover additional annual revenues of \$4,744,305 resulting from third-party purchased water and sewer treatment expenses, and \$6,987,498 resulting primarily from investments in infrastructure needed to serve customers, for a total requested annual revenue increase of \$11,731,803. With the plant investments the Company has made to maintain and improve its service to customers, and the increased operating expenses Blue Granite has experienced, it is unable to earn its authorized rate of return. At the time of the Application, the Company was earning only a 0.10% rate of return on an unadjusted basis, and a negative 3.0% rate of return on an adjusted basis.

In order to achieve more timely recovery of expenses going forward, and perhaps delay future rate cases, Blue Granite also seeks approval of a pass-through rate adjustment mechanism for third-party purchased water and sewer treatment expenses. Additionally, Blue Granite seeks approval of a Storm Reserve Fund, to assist in funding extraordinary storm recovery efforts, and approval of a "Round Up" program, whereby customers can voluntarily "round up" their bills to fund assistance for low income customers in meeting their utility bills. Blue Granite does not seek structural changes in its cost allocations and overall rate design in this proceeding, but has indicated that it is agreeable to preparing and presenting a full cost of service study in its next rate case.

Since the Company's last rate case, Blue Granite has invested approximately \$23 million in its water and wastewater systems in order to better serve its customers. These investments were necessary to (1) end the legal discharge of fully treated wastewater from the Friarsgate Wastewater

Treatment Facility into the Saluda River; (2) improve the water quality for customers receiving water from Stonegate's well water system; (3) ensure the sustainable provision of water to customers previously served by the failing Shandon wells; (4) support the growing Lake Wylie/Riverhills community through the addition of a secondary water connection; and (5) maintain and improve a number of wastewater collection systems across the Company's footprint.

These investments, along with a number of improvements instituted by the Company, demonstrate Blue Granite's recent change in strategy. Approximately two years ago the Company took a hard look at its performance and decided to make some significant changes in terms of personnel, capital budgets, infrastructure investments, and operating processes, in order to substantially improve Blue Granite's performance in these and other areas. The Company's testimony indicates that these efforts are underway and will continue, and that the performance improvements will take several years of sustained focus and investment. However, to date, the Company has implemented a number of changes and made a number of improvements to its systems for the benefit its customers. These include nearly tripling the level of annual capital investment in infrastructure, upgrading operations and management personnel, implementing a new operations management system, reorganizing the reporting structure, adopting standard operating procedures, instituting an incident command structure for storm response, instituting centralized procurement processes, implementing an online customer portal and app that allows customers to pay bills and check consumption online, instituting a community engagement and philanthropy plan, and implementing customer workshops throughout the state to provide regular in-person opportunities for customers to meet with Company personnel about rate, billing, and customer service questions.

On the infrastructure side, as mentioned above, the Company has completed the interconnection of Shandon and Carrolton Place systems, converted the Stonegate well water system to a purchased water system through interconnection with the city of Columbia, constructed a wastewater lift station at the Friarsgate wastewater treatment plant and interconnected the system with the City of Columbia, completed an additional water system connection with the City of Charlotte to serve its Lake Wylie service area, completed a series of wastewater collection system improvement projects, and constructed a new lift station in the Forty Love Subdivision. Additionally, the Company also recently completed the installation of advanced metering infrastructure in the Lake Wylie water system. Water supply and quality are improved, environmental compliance is improved, internal awareness of the Company's maintenance and investment needs is improved, and communications and customer experience is improved.

#### **IV. STATUTORY STANDARDS AND REQUIRED FINDINGS**

The evidence supporting Blue Granite's business and legal status is contained in its Application, testimony, and prior Commission Orders in the docket files of the Commission, of which the Commission takes judicial notice. Blue Granite is a corporation duly organized and existing under the laws of the State of Delaware, and is a public utility, as defined by S.C. Code Ann. § 58-5-10(4), providing water and sewer service to the public for compensation in certain areas of South Carolina. Blue Granite's operations in this State are subject to the Commission's jurisdiction over the Company's rates, charges, tariffs, and terms and conditions of service as generally provided in S.C. Code Ann. §§ 58-5-10 *et seq.*

The rates in effect prior to this order were approved in Commission Order No. 2018-802, Order on Rehearing, issued on January 25, 2019 in Docket No. 2017-292-WS. The historic test

year utilized for purposes of the Application is the twelve-month period ending June 30, 2019. Application ¶ 5. The Application, testimony, exhibits, affidavits of publication, public notices, and other filings submitted by Blue Granite are in compliance with the procedural requirements of the South Carolina Code of Laws and the Regulations promulgated by this Commission.

These findings of fact are informational, procedural and jurisdictional in nature, and the matters to which they relate are not contested by any party.

South Carolina Code Ann. § 58-5-210 authorizes the Commission “to ascertain and fix such just and reasonable standards, classifications, regulations, practices and measurements of service to be furnished, imposed, observed and followed by every public utility in this State . . . .” Rates are set using a historic test year, and the object of using test year figures is to reflect typical conditions. The company has the benefit of choosing its test year. Where an unusual situation indicates that the test year figures are atypical, the Commission should adjust the test year data. *Parker v. S.C. Pub. Serv. Comm’n*, 280 S.C. 310, 312, 313 S.E.2d 290, 292 (1984). The Commission must make adjustments for known and measurable changes in expenses, revenues, and investments so that the resulting rates will accurately and truly reflect the actual rate base, net operating income, and cost of capital. *Southern Bell Tel. & Tel. Co. v. Pub. Serv. Comm’n*, 270 S.C. 590, 602-03 (1978).

The Commission must determine a fair rate of return that the utility should be allowed the opportunity to earn after the recovery of its expenses of utility operations. The legal standards for this determination are set forth in *Federal Power Comm’n v. Hope Natural Gas Co.*, 320 U.S. 591, 602-03(1944) (“*Hope*”) and *Bluefield Water Works and Improvement Co. v. Public Service Commission of West Virginia*, 262 U.S. 679, 692-93 (1923) (“*Bluefield*”).

*Bluefield* holds that:

What annual rate will constitute just compensation depends upon many circumstances, and must be determined by the exercise of a fair and enlightened judgment, having regard to all relevant facts. A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures. The return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate, under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties. A rate of return may be reasonable at one time and become too high or too low by changes affecting the opportunities for investment, the money market and business conditions generally.

*Bluefield*, 262 U.S. at 692-93. This Commission and the South Carolina courts have consistently applied the principles set forth in *Bluefield* and *Hope*. Quoting *Hope*, the South Carolina Supreme Court has held: “Under the statutory standard of ‘just and reasonable’ it is the result reached not the method employed which is controlling . . . . The ratemaking process under the Act, i.e., the fixing of ‘just and reasonable’ rates, involves the balancing of investor and the consumer interests.” *Southern Bell*, 270 S.C. at 596 (quoting *Hope*, 320 U.S. at 602-03).

As related to these matters, the South Carolina Supreme Court has reasoned as follows: “the fixing of ‘just and reasonable’ rates involves the balancing of the investor and the consumer interests . . . .” *Southern Bell*, 270 S.C. at 596-97 (quoting *Hope*, 320 U.S. at 602-03).

This Commission must exercise its dual responsibility of permitting utilities an opportunity to earn a reasonable return on the property it has devoted to serving the public, on the one hand, and protecting customers from rates that are so excessive as to be unjust or unreasonable, on the other, by “(a) [n]ot depriving investors of the opportunity to earn reasonable returns on the funds

devoted to such use as that would constitute a taking of private property without just compensation[, and] (b) [n]ot permitting rates which are excessive.” *Southern Bell*, 270 S.C. at 605. Ultimately, this balancing act takes place within the context of a utility setting forth proposed rates—pursuant to Title 58, Chapter 27, Article 7 of the S.C. Code of Laws—for the purpose of the utility receiving revenue sufficient to yield a reasonable return.

Additionally, the Commission’s determination of a fair rate of return must be documented fully in its findings of fact and based exclusively on reliable, probative, and substantial evidence on the whole record. *Porter v. S.C. Pub. Serv. Comm’n*, 504 S.E.2d 320, 323 (1998).

Practically, although the burden of proof in showing the reasonableness of a utility’s costs that underlie its request to adjust rates ultimately rests with the utility, the S.C. Supreme Court has concluded that the utility is entitled to a presumption that its expenses are reasonable and were incurred in good faith. *Hamm v. S.C. Pub. Serv. Comm’n*, 309 S.C. 282, 286, 422 S.E. 110, 112 (1992). However, according to *Utils. Servs. of S.C., Inc. v. S.C. Office of Regulatory Staff*, 392 S.C. 96, 110, 708 S.E.2d 755, 762-63 (2011), “if an investigation initiated by ORS or by the PSC yields evidence that overcomes the presumption of reasonableness, a utility must further substantiate its claimed expenditures.”

The Commission’s Findings of Facts and Conclusions reflect these standards.

## **V. REVIEW OF THE EVIDENCE AND EVIDENTIARY CONCLUSIONS**

### **A. Areas of Agreement and Compromise**

In its rebuttal testimony, Blue Granite indicated it is willing to agree and compromise with the following ORS proposed adjustments:

- Adjustments 1, 2, 3, 4, and 26b regarding pro forma present rate revenues, Uncollectible Expense, and Gross Receipts Tax.
- Adjustments 5, 6, 14, 17a, and 26a related to Salaries & Wages, Capitalized Time, and Payroll Taxes.
- Adjustment 9a related to deferred maintenance.
- Adjustments 9b, 13a, and 20 related to the Clearwater Solutions Midlands region contract.
- Adjustments 9e, 13b, 15a, 15c, 21d, and 23b for rebranding and non-allowable expenses.
- Adjustment 19 for Insurance Expense.
- Adjustment 21a for Corix parent cost allocations.
- Adjustments 16a, 21c, and 21e regarding regulatory commission expenses and legal expenses, subject to the recommendation detailed later in my testimony.
- Adjustment 37 regarding Plant Held for Future Use.
- The calculations for Adjustments 27, 28, 35a, 35b, and 39 regarding Income Taxes, Cash Working Capital, and Interest Expense, subject to the results of adjustments elsewhere that impact these figures.

The Company also agrees with the ORS update of the as-filed Tax Cuts and Jobs Act one-time credit to customers, based on adjusted pro forma customer counts. Blue Granite also appears to be in agreement with ORS on several items which were not adjusted by ORS from the Company's filed application, specifically Adjustments 7, 10, 11a, 11b, 12a, 12b, 21b, 22, 23a, 29, 30, and 31.



## **B. Areas of Dispute**

The areas of dispute are addressed below.

### **i. Cost of Capital**

As discussed below, we find and conclude that Mr. D’Ascendis’ recommended cost of equity of 10.25% for Blue Granite is reasonable and should be approved based upon our analysis and findings concerning the ROE methodologies, inputs, and assumptions, and also based on our view that the DCF method should be given relatively less weight, our view that the ECAPM method should be given consideration, our view that Blue Granite’s company-specific risks are relevant and support an ROE at the higher end of a reasonable range of ROEs, and evidence of the need for the Company to maintain financial integrity in light of its ongoing capital financing needs.

### **Company Proposal**

Blue Granite witness Dylan D’Ascendis, a Director at ScottMadden, Inc., testified concerning the Company’s cost of capital. Mr. D’Ascendis supported a cost of capital of between 7.86% and 8.12%, based on the Company’s actual capital structure at June 30, 2019 (52.91% equity and 47.09% debt), the Company’s actual cost of long-term debt (5.73%), and a cost of equity between 9.75% and 10.25%. (Tr. p. 547.4; 547.37, updated in Rebuttal Testimony.)

No party disputed the use of the Company’s actual capital structure as of June 30, 2019 or the Company’s actual cost of long-term debt; the disagreements relate to the estimate of the Company’s cost of equity.

Mr. D’Ascendis calculated the Company’s cost of equity by applying several well-known cost of equity models -- the Discounted Cash Flow Model (“DCF”), the Risk Premium Model (“RPM”), the Capital Asset Pricing Model (“CAPM”) – to the market data of a proxy group of

water utility companies and to a proxy group of domestic, non-price regulated with comparable risk to the utility proxy group. These analyses produced a cost of equity estimate of 9.75%. He then applied a 0.50% upward adjustment to account for Blue Granite's small size. (Tr. p. 547.5-6; updated in Rebuttal Testimony.)

Mr. D'Ascendis emphasized the importance of using multiple cost of equity models to determine a utility's cost of equity, because no single model is so inherently precise that it can be relied on solely to the exclusion of other theoretically sound models. He noted that the use of multiple models adds reliability to the estimation of the cost of equity rate, and the prudence of using multiple cost of equity models is supported in both financial literature and regulatory precedent. (Tr. p. 547.37.)

With regard to his DCF analysis, Mr. D'Ascendis used a dividend yield adjustment and growth rate assumptions based on analysts' five-year forecasts of earnings per share growth. Mr. D'Ascendis' DCF results indicated a cost of equity of 8.91% for the water utility proxy group. (Tr. p. 547.16-19; updated in Rebuttal Testimony.)

With regard to his RPM analysis, Mr. D'Ascendis relied on two risk premium methods – the Predictive Risk Premium Model ("PRPM") and a risk premium approach using a total market approach – and estimated a cost of equity of 10.21% for the water utility proxy group. Under the PRPM method, Mr. D'Ascendis used a consensus forecast of the 30-year Treasury Bond yield plus an equity risk premium calculated from a variance of historical risk premiums. His total market approach was based on a consensus forecast of a prospective public utility bond yield plus an average equity risk premium derived from a beta-adjusted total market equity risk premium and

an equity risk premium based on the S&P Utilities Index. (Tr. p. 547.18-28; updated in Rebuttal Testimony.)

Mr. D’Ascendis’ CAPM analysis was based on an average of both the CAPM and the ECAPM (“Empirical CAPM”) analyses, and produced a cost of equity estimate of 9.10% for the water utility proxy group. His CAPM analysis estimated the risk premium derived from an average of Ibbotson-based market risk premiums, Value Line data-based market risk premiums, and Bloomberg data-based market risk premiums. (Tr. p. 547.28-34; updated in Rebuttal Testimony.)

Mr. D’Ascendis’ application of these cost of equity methodologies to the comparable risk, non-price regulated companies indicated a cost of equity of 11.16%. (Tr. p. 547.34-37; updated in Rebuttal Testimony.)

Based on the results of his analyses, the average of the mean and the median of all of the model results produces an unadjusted estimated cost of equity of 9.75%. Mr. D’Ascendis then made an upward adjustment of 0.50% to reflect Blue Granite’s greater business risk due to its unique risks as well as its small size relative to the proxy group, resulting in his recommended cost of equity of 10.25% for Blue Granite. (Tr. p. 547.37-4; updated in Rebuttal Testimony.)

### **ORS Position**

David Parcell, a principal and senior economist with Technical Associates, Inc., testified on behalf of ORS on cost of capital issues. He recommended a cost of equity of 9.45% and an overall weighted cost of capital of 7.70%, using the same capital structure and cost of long-term debt as did the Company. (Tr. p. 1004.3; 1004.37.)

To estimate the Company's cost of equity, Mr. Parcell employed the following three methodologies: DCF, CAPM, and Comparable Earnings (“CE”). Based upon his use of these

models, he concluded that the Company's cost of equity is within a range of 8.9% to 10.0% (9.45% being the midpoint), which is based upon the upper end of his DCF results and the upper end of his CE results. He stated that he used the upper ends of his DCF and CE ranges in order to give consideration to any perceived unique attributes of Blue Granite. (Tr. p. 1004.3-4.)

Mr. Parcell utilized substantially the same water utility proxy group as did Mr. D'Ascendis. In his DCF analysis, he utilized a combination of current and projected dividend yields. He relied equally on the results of his DCF model and CE model. (Tr. p. 1004.4; 1004.20; 1004.25.)

With respect to his CAPM analysis, Mr. Parcell's indicated return was 6.20%, which he explains as a result of market risk premiums being lower than in recent years and a result of interest rates on U.S. Treasury bonds being lower in recent years. Due to his low CAPM result, he does not consider his CAPM results in the determination of his final cost of common equity range. He also uses current, rather than projected, yields on 20-year U.S. Treasury bonds, uses both geometric and arithmetic mean returns, and uses historical mean total return on U.S. Treasury securities, in his CAPM analysis. Mr. Parcell did not perform an ECAPM analysis as Mr. D'Ascendis did. (Tr. p. 1004.25-31.)

With regard to his CE analysis, Mr. Parcell relies on a direct relationship between market-to-book ratios, and used his utility proxy group plus the S&P 500 index. (Tr. p. 1004.31-36.)

Mr. Parcell made no adjustments to reflect an increased risk to Blue Granite due to its smaller size. However, he did select the high ends of his ranges of DCF and CE cost rates to reflect the "perceived unique attributes of [Blue Granite]." (Tr. p. 1004.4.) Based upon those "unique attributes" and because—in his view—the "DCF results are low by historic standards," Mr. Parcell selected the higher end of his range. (Tr. p. 1015.)

In surrebuttal testimony, Mr. Parcell addressed Mr. D’Ascendis’ criticisms of his DCF, CAPM, and CE analyses, including the use of 20-year Treasury bond yields and forecasted rather than current yields. (Tr. p. 1005.2-14.)

**Consumer Advocate Position**

Aaron Rothschild, President of Rothschild Financial Consulting, testified on cost of capital issues on behalf of the Consumer Advocate. He recommended an overall cost of capital for Blue Granite of 7.27%, based on a cost of equity of 8.47%, a 28-basis point upward adjustment to the ROE for size, a 10-basis point downward adjustment to the ROE for financial risk, a capital structure containing 52.91% of common equity and 47.09% of debt, and a debt cost rate of 5.73%. In arriving at his return on equity recommendation for Blue Granite, Mr. Rothschild employed a DCF Model, a Non-Constant Growth DCM Model, and a CAPM analysis. (Tr. p. 672.4-8.)

According to Mr. Rothschild, the primary reasons for the differences between Mr. Rothschild’s and Mr. D’Ascendis’ estimated cost of equity for the Company stem from: (1) Mr. Rothschild’s use of a proxy group that excludes Mr. D’Ascendis’ non-price regulated companies, due to his belief that such companies are not sufficiently comparable; (2) Mr. Rothschild’s use of a lower risk premium than Mr. D’Ascendis, based on his view that market-based return expectations are lower than the risk premium assumed by Mr. D’Ascendis. (Tr. p. 672.9-13.)

In arriving at his ROE recommendation for Blue Granite, Mr. Rothschild gives equal weight to his Constant Growth DCF, Non-Constant Growth DCF, and CAPM analyses. Mr. Rothschild testified that his recommended return on equity of 8.65% is reasonable, due to the fact that stocks are expensive; interest rates are low; credit spreads are low; and volatility expectations are relatively low (based on the “VIX” Market Volatility Index). (Tr. p. 672.13-15.)

In surrebuttal testimony, Mr. Rothschild responded to Mr. D’Ascendis’ testimony concerning his market-based approach as opposed to expert forecasts, his use of short-term analyst forecasts in connection with his DCF analysis, his methodology for estimating projected growth in a DCF model, his reliance on authorized ROEs for other companies in his DCF analysis, and other aspects of his DCF analyses. Mr. Rothschild also responded to Mr. D’Ascendis’ testimony addressing his CAPM analysis, such as his use of current rather than forecasted interest rates, his use of option-implied betas, and his failure to use the ECAPM. (Tr. p. 683.5-26.)

### **York County Position**

Erik Rekitt, York County Public Works Assistant Director, also testified on return on equity issues. He addressed Mr. D’Ascendis’ testimony concerning the age of pipes, stating that the Lake Wylie Franchise Territory has no water and sewer lines approximating 75 to 100 years of age. He also took issue with the reference to “divestment or withdrawal” in Mr. D’Ascendis’ testimony. Finally, he took issue with Mr. D’Ascendis’ proxy group because it relies upon six companies with little or no relevance to South Carolina. (Tr. p. 1029.5.)

### **Company Response**

In rebuttal testimony, Mr. D’Ascendis responded to Mr. Parcell’s testimony, focusing on his undue weighting of his DCF results, his misapplication of the CAPM model, his misapplication of the CE model, and his failure to account for Blue Granite’s size-specific risks over and above the range of ROEs indicated by his proxy groups. (Tr. p. 548.4-5.)

With respect to the weighting of DCF results, Mr. D’Ascendis pointed to academic and mathematical evidence indicating that DCF Model results should be viewed with caution at this

time due to the fact that market-to-book ratios are currently extraordinarily high compared to the ten-year average. (Tr. p. 548.7-12.)

With respect to the CAPM, Mr. D’Ascendis stated that Mr. Parcell’s CAPM result of 6.20% is unreasonable on its face, and testified that Mr. Parcell’s incorrect use of inputs in the application of the CAPM is the driving factor behind this unreasonable result. Mr. D’Ascendis stated that Mr. Parcell’s CAPM analysis is flawed in at least three respects: first, he relied on an historical, recent risk-free rate despite the fact that ratemaking and cost of capital are prospective; second, he incorrectly calculated the market risk premium by relying on achieved (non-market based) rates of return on book common equity for the S&P 500, a geometric mean historical market equity risk premium, and the historical total return on U.S. Treasury bonds; and third, he did not incorporate an ECAPM analysis even though empirical evidence indicates that low-beta securities (such as utilities) earn returns higher than the CAPM predicts and high-beta securities earn less. (Tr. p. 548.13-25.)

With respect to the CE analysis, Mr. D’Ascendis criticized Mr. Parcell’s misplaced reliance on a direct relationship between market-to-book ratios and earnings on book common equity, noting that neither academic literature nor historical analysis supported such. Mr. D’Ascendis also criticized Mr. Parcell’s failure to consider non-price regulated companies in his comparable earnings analysis. (Tr. p. 548.26-31.)

Mr. D’Ascendis also disagreed with Mr. Parcell’s failure to make an adjustment outside of the proxy group ROE range to reflect Blue Granite’s relative smaller size. Mr. D’Ascendis pointed to analytical evidence supporting the increased risk to Blue Granite stemming from its smaller size. (Tr. p. 548.32-39.)

Mr. D’Ascendis also responded to Mr. Rothschild’s testimony in rebuttal, focusing on current and expected capital market conditions, his misapplication of DCF models, his misapplication of the CAPM, and the downward adjustment to his indicated ROE for financial risk. Mr. D’Ascendis emphasized that Mr. Rothschild’s recommended ROE, if approved, would be the lowest ROE approved for a water / wastewater utility in the U.S. He explained that he disagreed with Mr. Rothschild in several principal areas, including the interpretation of current and expected market conditions, undue weight given to the DCF models, misapplication of both his constant growth and non-constant growth DC models, his application of the CAPM, and his financial risk adjustment. With regard to the financial risk adjustment, Mr. D’Ascendis pointed out the proxy group’s equity ratio is nearly identical to Blue Granite’s. (Tr. p. 548.44-72.)

### **Commission Findings**

The U.S. Supreme Court established the guiding principles for establishing a fair return for capital in two seminal cases: (1) *Bluefield Water Works and Improvement Co. v. Public Service Comm’n* (“Bluefield”); and (2) *Federal Power Comm’n v. Hope Natural Gas Co.* (“Hope”). In *Bluefield*, the Court stated:

A public utility is entitled to such rates as will permit it to earn a return upon the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures. The return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate, under efficient and economical management, to maintain and support its credit, and enable it to raise the money necessary for the proper discharge of its public duties.



The Court thus recognized that: (1) a regulated public utility cannot remain financially sound unless the return it is allowed to earn on its invested capital is at least equal to the cost of capital; and (2) a regulated public utility will not be able to attract capital if it does not offer investors an opportunity to earn a return on their investment equal to the return they expect to earn on other investments of similar risk.

In *Hope*, the Court reiterated the financial integrity and capital attraction principles of the *Bluefield* case:

From the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and dividends on the stock. . . . By that standard the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.

In summary, the Court clearly has recognized that the fair rate of return on equity should be: (1) comparable to returns investors expect to earn on other investments of similar risk; (2) sufficient to assure confidence in the company's financial integrity; and (3) adequate to maintain and support the company's credit and to attract capital. As discussed previously, South Carolina precedent comports with the *Hope* and *Bluefield* principles.

Based on the *Hope* and *Bluefield* standards, the ROE authorized in this proceeding should provide the Company with the opportunity to earn a fair and reasonable return, and enable efficient access to external capital under a variety of market conditions. A return that is adequate to attract capital at reasonable terms enables the utility to provide service while maintaining its financial integrity. As discussed above, and in keeping with the *Hope* and *Bluefield* standards, that return should be commensurate with the returns expected elsewhere in the market for investments of

equivalent risk – and not just utility investments. The consequence of the Commission’s order in this case, therefore, should be to provide Blue Granite with the opportunity to earn an ROE that is: (1) adequate to attract capital at reasonable terms; (2) sufficient to ensure its financial integrity; and (3) commensurate with returns on investments in enterprises having corresponding risks. To the extent Blue Granite is provided a reasonable opportunity to earn its cost of equity, neither customers nor shareholders should be disadvantaged. In fact, a return that is adequate to attract capital at reasonable terms enables Blue Granite to provide safe, reliable utility service while maintaining its financial integrity, all to the benefit of both investors and customers.

Notably, the parties were in agreement with respect to the appropriate capital structure and cost of long-term debt to use in this case to calculate Blue Granite’s cost of capital. The disagreements concern the estimated cost of equity.

In order to meet the requirements set forth in *Bluefield* and *Hope*, the parties proposed various returns using a variety of methods as bases for their positions on the Company’s cost of equity. Based on the entirety of the testimony presented on this issue, it is apparent that we have been presented with, in several instances, highly detailed discussions of the cost of equity capital. Among other things, our discussion and analysis of this issue serves to illustrate that the goals for setting the fair rate of return for a public utility go well beyond the use of formulas and mathematical calculations which may imply a level of precision which does not really exist. With this in mind, we turn our analysis to the cost of equity evidence submitted in this proceeding.

Many of the witnesses testifying concerning the Company’s cost of capital used similar approaches – various types of DCF studies, the CAPM model, Risk Premium approaches, and Comparable Earnings analyses. As is typically the case, however, they came to different

conclusions. Mr. D'Ascendis' recommended range of reasonable ROEs for Blue Granite is 9.75% to 10.25%, with a point recommendation of 10.25% based on a 50-basis point upward size adjustment. Mr. Parcell testified to a range of ROEs from 8.9% to 10.0% and recommended a 9.45% ROE for Petitioner. Mr. Rothschild testified to a recommended an ROE of 8.65%. Mr. Rekitt offered testimony on the subject of return on equity, but made no specific recommendations.

Thus, the cost of equity calculations presented in this case range from 8.65% to 10.25% -- a range of 160 basis points. Notably, the non-utility parties' ranges of ROEs went from a low of 8.65% to a high of 10.0% -- 135 basis points. Several factors, some of which are discussed in more detail below, contributed to the variation in estimates. While we do not find it necessary to resolve each of the sometimes academic disagreements between the witnesses, we discuss below the major areas of disagreement. At the outset, however, we note that we find Mr. Rothschild's recommended cost of equity of 8.65% outside the bounds of reasonableness, as judged by both a review of recently-authorized ROEs in other cases as well as the testimony of other witnesses in this proceeding.

The primary areas of disagreement among the witnesses are as follows: (1) the appropriate weighting for the different methods, particularly in the current capital environment; (2) the use of historic and current data versus projected data; (3) the importance of an ECAPM analysis in this capital and market environment; (4) the importance of company-specific risks such as size; and (5) the importance of maintaining financial integrity of the utility.

With regard to the weight to be given the various models, we continue to believe that each approach is useful and should be considered. However, we are persuaded that Mr. D'Ascendis is

correct in his recommendation that we give relatively less weight to the Constant Growth DCF results in the current capital market environment. As the evidence makes clear, the DCF results are markedly below what we and other regulatory commissions have recently found to be reasonable estimations of the cost of a utility's equity. For example, Mr. Rothschild's DCF results range from 5.72% to 8.76%. Mr. Parcell's DCF results range from 8.2% to 8.9%. And Mr. D'Ascendis' DCF result of 8.91% is the lowest of his model results. We note that in 2018, the FERC found that "in light of current investor behavior and capital market conditions, relying on the DCF methodology alone will not produce a just and reasonable ROE." *See* Docket Nos. EL14-12-003 and EL15-45-000, *Order Directing Briefs*, 165 FERC ¶ 61,118 (November 15, 2018) at para. 34. *See also* Docket No. EL11-66-001, *et al.*, *Order Directing Briefs* 165 FERC ¶ 61,030 (October 16, 2018) at para. 30.

And in its July 2017 Order Accepting Stipulation in which it authorized a 9.90% ROE for Duke Energy Carolinas, the North Carolina Utilities Commission noted it "carefully evaluated the DCF analysis recommendations" of the ROE witnesses (which ranged from 8.45 % to 8.80%) and determined that "all of these DCF analyses in the current market produce unrealistically low results. The fundamental structure of the Constant Growth DCF model assumes constancy in perpetuity, which is simply not compatible with the recent and current capital markets and economic environment. Accordingly, we conclude that we should give relatively less weight to the Constant Growth DCF model. Notably, this conclusion is consistent with our longstanding view that the cost of equity cannot be precisely calculated and estimating it requires the use of judgment; due to this lack of precision, the use of multiple methods is desirable because no single method will produce the most reasonable result under all conditions and circumstances." State of North

Carolina Utilities Commission, Docket No. E-7, Sub 1146, *In the Matter of Application of Duke Energy Carolinas, LLC, for Adjustment of Rates and Charges Applicable to Electric Utility Service in North Carolina*, Order Accepting Stipulation, Deciding Contested Issues, and Requiring Revenue Reduction, July 25, 2017, at 62. Indeed, we have previously determined that “it is appropriate and reasonable to consider a range of estimates under various methodologies in order to more accurately estimate [a utility’s] cost of equity,” and relying on a single analytical method is “inconsistent with decisions reached by regulatory commissions over the past several years and departs from the normal practice of estimating the Cost of Equity for utilities.” Public Service Commission of South Carolina, Docket Nos. 2017-207-E, 2017-305-E, and 2017-370-E, Order No. 2018-804, *Order Addressing South Carolina Electric & Gas Nuclear Dockets*, at 89-90.

Within the context of our consideration of the DCF model, we are persuaded that Mr. D’Ascendis’ growth rate assumptions are the most reasonable. His growth rate estimates are based on analysts’ growth rate estimates, which are both forward-looking and relied upon by investors. Our task in estimating cost of equity is focused on returns required by investors, which in turn is focused on investors’ expectations.

Similarly, with regard to the risk-free rate input for the CAPM, we agree with Mr. D’Ascendis that because the cost of equity is forward-looking, it also is important to reflect forward-looking expectations of the risk-free rate. We also agree that the risk-free rate assumption should reflect the fact that utility equity is a long-term investment. Accordingly, we agree with his use of long-term U.S. Treasury bonds. As Mr. D’Ascendis testified, the 30-year Treasury yield best matches the life of the underlying investment – because utility securities and utility rate base are typically long duration investments.

With respect to the Beta coefficient input for the CAPM, we agree with Mr. D’Ascendis: the evidence and academic experts indicate the CAPM tends to underestimate returns for firms with low-Beta coefficients. As Mr. D’Ascendis explained, the ECAPM adjusts for the CAPM’s tendency to under-estimate returns for companies that have Beta coefficients less than one (like utilities), and over-estimate returns for relatively high-Beta coefficient stocks. The ECAPM recognizes the results of academic research indicating that the risk-return relationship is different (flatter) than estimated by the CAPM. We note that, as Dr. Roger Morin has stated, the ECAPM is “a formal recognition that the observed risk-return tradeoff is flatter than predicted by the CAPM based on myriad empirical evidence. . . . Even if a company’s beta is estimated accurately, the CAPM still understates the return for low-beta stocks. . . . [T]he ECAPM is a return [] adjustment and not a beta [] adjustment. Both adjustments are necessary.” (Tr. p. 548.23-24.) Because the ECAPM mitigates the drift in Beta coefficients, we agree it is a reasonable method to use, and we find that Mr. D’Ascendis’ use of the ECAPM and his Beta coefficient inputs are reasonable.

We next address the Equity Risk Premium input for the Bond Yield Plus Risk Premium model. We conclude, as does Mr. D’Ascendis, that because the cost of equity is forward-looking, it is appropriate to use projected Treasury yields in the analysis. Those inputs produce reasonable estimates of the cost of equity.

Similarly, we share Mr. D’Ascendis’ concerns regarding the use of historical earned rates of return in the Comparable Earnings analysis, due to the fact the cost of equity is inherently forward-looking. We agree that using future expected returns supports Mr. D’Ascendis’ analysis much more than it does other witnesses.

Next we consider the importance of considering company-specific risks in our cost of equity analysis. Mr. Parcell and Mr. Rothschild to a degree urge us to ignore company-specific risks. Mr. D’Ascendis, on the other hand, persuasively argues that Blue Granite faces unique risks that the proxy group companies do not face, namely, its relatively smaller size and its increasing regulatory risk. We agree with Mr. D’Ascendis that company-specific risk is highly relevant to the determination of cost of equity. We note that the financial community pays close attention to regulation when it rates specific utility companies, and their analyses influence investment decisions. Accordingly, we agree with Mr. D’Ascendis that it is important that we qualitatively consider the company-specific risks when determining Blue Granite’s cost of equity. On balance, these company-specific risks generally support an ROE at the higher end of a reasonable range of ROEs for Blue Granite, and specifically support Mr. D’Ascendis’ 50-basis point upward adjustment within his range of recommended ROEs.

We would also be remiss if we did not also consider the importance of the utility’s financial integrity when making our cost of equity determination. As the Company’s case-in-chief testimony indicates, Blue Granite is currently earning virtually no return on its capital employed in providing water and wastewater services to its South Carolina customers. At the same time, Blue Granite faces the need to make additional capital investments of the benefit of its customers, at a relatively small size and in a somewhat uncertain legislative environment. It is important, and beneficial, to customers that the Company be able to finance needed investments on reasonable terms. Indeed, *Hope* and *Bluefield* and South Carolina precedent require us to take actions to maintain utilities’ financial integrity.

Given the foregoing, we conclude and find that Mr. D’Ascendis’ recommended cost of equity of 10.25% for Blue Granite is reasonable and should be approved. Our finding is supported not only by our analysis and findings concerning the ROE methodologies, inputs, and assumptions, but also by our view that the DCF method should be given relatively less weight, our view that the ECAPM method should be given consideration, our view that Blue Granite’s company-specific risks are relevant and support an ROE at the higher end of a reasonable range of ROEs, and evidence of the need for the Company to maintain financial integrity in light of its ongoing capital financing needs.

Accordingly, for purposes of this Cause, we find that the Company’s overall cost of capital is 8.12%, computed as follows:

Description	Ratio	Cost	Weighted Cost
Common Equity	52.91%	10.25%	5.42%
Long Term Debt	47.09%	5.73%	2.70%
Total	100.00%		8.12%

## **ii. Depreciation Rates**

As discussed below, we find that Mr. Spanos’ proposed service lives and net salvage estimates are the most reasonable and should be approved, based upon his expertise in the field, including his expertise with water and wastewater depreciation studies; the presentation of his depreciation studies and the rationales therefor; and his approach of combining mathematical calculations with the application of expert professional judgment and visual curve fitting techniques.

### **Company’s Proposal**

Blue Granite witness DeStefano testified that the Company has not prepared a depreciation study, nor has it updated its depreciation rates, for a number of years. As a result, he stated, the



current depreciation rates are outdated, and are premised upon unrealistically long depreciable lives for facilities and equipment. Further, he stated, the current rates also reflect a similar useful life across virtually all asset classes, which is not realistic when considering the significant recent and anticipated asset replacements implemented by the Company and the nature and variety of infrastructure and equipment employed. For these reasons, the Company engaged John Spanos of Gannett Fleming to prepare a depreciation study and recommend updated depreciation rates that better reflect the reasonable life cycle of the Company's assets and better align cost recovery for the assets providing service to the customers receiving the benefits of such infrastructure. In addition, Mr. DeStefano explained, Mr. Spanos has proposed a cost of removal component to various depreciation rates to accommodate decommissioning and other removal costs related to asset retirements. He testified that implementation of cost of removal rates will mitigate the need to request deferral of such incurred costs in future proceedings, as well as better reflect appropriate regulatory cost matching principles, pairing cost recovery with the customers who benefit from the asset during its useful life. (Tr. p. 763.9-10.)

John J. Spanos, President, Gannett Fleming Valuation and Rate Consultants, LLC, a longstanding depreciation expert, testified about the results of his review and analyses of Blue Granite's plant in-service, conducted in the process of preparing depreciation studies of the Company's water and wastewater plant assets as of December 31, 2018. He explained that depreciation, as applied to depreciable public utility plant, means the loss in service value not restored by current maintenance, incurred in connection with the consumption or prospective retirement of utility plant in the course of service from causes which are known to be in current operation against which the Company is not protected by insurance. Among the causes to be given

consideration are wear and tear, decay, action of the elements, inadequacy, obsolescence, changes in the art, changes in demand, and the requirements of public authorities. (Tr. p. 537.5.)

Mr. Spanos testified that depreciation rates are affected by service life and net salvage parameters. He stated that these parameters are determined based on a combined statistical analysis and informed judgment of each asset class. He stated that informed judgments of each asset class are developed based on field inspections and discussions with management with regard to plans and outlook of assets. Mr. Spanos testified that based on his depreciation studies, the composite rate for water assets is 4.06%, and the composite rate for wastewater assets is 3.32%. He opined that the proposed depreciation rates resulting from his depreciation studies are reasonable and appropriate given that they incorporate the service life and net salvage parameters currently anticipated for each of the Company's property group investments over their average remaining lives. (Tr. p. 537.5-6.)

Mr. Spanos testified that he used the straight line remaining life method of depreciation, with the average service life procedure to develop recommended depreciation accrual rates. The total annual depreciation is based on a system of depreciation accounting which aims to distribute the cost of fixed capital assets over the estimated useful life of the unit, or group of assets, in a systematic and rational manner. He explained that, for certain accounts for which depreciation accounting would be difficult, he used amortization accounting. (Tr. p. 537.6; 537.9-10.)

Mr. Spanos explained that the determination of annual depreciation accrual rates consists of two phases. In the first phase, service life and net salvage characteristics are estimated for each depreciable group, that is, each plant account or subaccount identified as having similar characteristics. In the second phase, he explained, the annual depreciation accrual rates are

calculated based on the service life and net salvage estimates determined in the first phase. (Tr. p. 537.6.)

Mr. Spanos testified that the service life and net salvage study consisted of compiling historical data from records related to the Company's plant; analyzing the data to obtain historical trends of survivor and salvage characteristics; obtaining supplementary information from management and operating personnel concerning the Company's practices and plans as they relate to plant operations; and interpreting the above data to form judgments of average service life and net salvage characteristics. (Tr. p. 537.7.)

He stated that the historical data consisted of the entries made by the Company to record plant transactions through 2018. The transactions included additions, retirements, transfers and the related balances. The Company, in accordance with Mr. Spanos' instructions, classified the data by depreciable group, type of transaction, the year in which the transaction took place, and the year in which the plant was installed. He noted that there were some installation years that required engineering personnel identification. (Tr. p. 537.7.)

He stated that he used the retirement rate method to analyze the service life data. That method is the most appropriate when aged retirement data are available, he testified, because it develops the average rates of retirement actually experienced during the period of study. Other methods of life analysis infer the rates of retirement based on a selected type survivor curve. He testified that each retirement rate analysis resulted in a life table which, when plotted, formed an original survivor curve. Each original survivor curve as plotted from the life table represents the average survivor pattern experienced by the several vintage groups during the experience band studied. He stated that, inasmuch as this survivor pattern does not necessarily describe the life

characteristics of the property group, interpretation of the original curves is required in order to use them as valid considerations in service life estimation. He stated that Iowa type survivor curves were used in these interpretations. More specifically, he explained that the Iowa curves and truncated Iowa curves were used in this study to describe the forecasted rates of retirement based on the observed rates of retirement and the outlook for future retirements. (Tr. p. 537.7-9.)

He testified that each net salvage data percentage is the combination of cost of removal and gross salvage as a percent of the original cost retired. There is no historical data to analyze, therefore, all estimates were based on informed judgment which included net salvage percentages of other water and wastewater utilities. He stated that the estimates are consistent with how the Company will record these costs going forward. (Tr. p. 537.9.)

With regard to the second phase of the process – calculation of the annual depreciation accrual rates -- Mr. Spanos testified that after he estimated the service life and net salvage characteristics for each depreciable group, he calculated annual depreciation accrual rates for each group in accordance with the straight line remaining life method, using the average service life procedure for all depreciable accounts and installation years. Mr. Spanos explained that, with regard to certain accounts, amortization accounting was used instead of depreciation accounting, due to the large number of units in such accounts and the concomitant difficulty of properly reflecting plant in-service without periodic inventories. He stated that in amortization accounting, units of property are capitalized in the same manner as they are in depreciation accounting; however, retirements are recorded when a vintage is fully amortized rather than as the units are removed from service. In other words, there is no dispersion of retirements; all units are retired when the age of the vintage reaches the amortization period. (Tr. p. 537.9-10.)

**ORS Position**

David J. Garrett, Managing Member, Resolve Utility Consulting, PLLC, testified on behalf of the ORS on depreciation issues. Mr. Garrett testified that he employed a depreciation system using actuarial plant analysis to statistically analyze the Company's depreciable assets and develop reasonable depreciation rates and annual accruals. He is of the opinion that the Company has not met its burden of showing that its proposed service lives and net salvage rates for many of its depreciable accounts do not result in excessive depreciation expense for customers. Specifically, Mr. Garrett testified that the service lives proposed by Mr. Spanos for several of the plant accounts in the depreciation studies are too short given the evidence supporting such service life proposals. Additionally, he stated, the net salvage rates proposed by Mr. Spanos are for several accounts in the depreciation studies, lower than what is otherwise indicated by the evidence provided (if any) to support the proposed net salvage rates. He stated that unreasonably short service lives and unreasonably low net salvage rates both contribute to the unreasonably high depreciation rates proposed by the Company. The ORS proposes a combination of longer service lives and/or higher net salvage rates on several of the Company's water and wastewater accounts. Mr. Garrett testified that, based on the empirical evidence provided by the Company in this case, the depreciation rates proposed in his testimony are more accurate than those proposed in the Company's depreciation study. As the Company accumulates more accurate data over time, he stated, depreciation rates should be updated periodically based on that data. On cross-examination, Mr. Garrett confirmed that he had only testified in one other water/wastewater rate case, in Indiana, and he stated that he had not performed any field inspections in connection with his depreciation studies in this case. (Tr. p. 1054.5-8; 1063-64.)

In surrebuttal testimony, Mr. Garrett noted that generally, he and Company witness Spanos both agree that there should be an increase in depreciation rates for Blue Granite. He stated that the Company's current depreciation rates are based on a composite average service life of about 66.67 years for all assets. He noted that the historical data and other evidence provided by the Company indicate that the average service lives for the assets in most of its accounts should be shorter than this. Likewise, he testified, both he and witness Spanos agree that there should be a net salvage component to depreciation rates. However, he reiterated that he believes the Company's requested increase is unreasonably excessive, especially in consideration of the evidence provided to support the proposed increase, with respect to service life and net salvage estimates. (Tr. p. 1055.2-3.)

In surrebuttal, Mr. Garrett also took issue with Mr. Spanos' testimony that his life estimates are based solely on mathematical best fitting curves and that he does not incorporate visual curve fitting techniques. He testified that sometimes he may select the best mathematically fitting curve, but not before incorporating visual curve fitting techniques and professional judgment. Further, he stated that often, the Iowa curve he selects is shorter than the best mathematically fitting curve, which means that his incorporation of professional judgment and visual curve fitting techniques actually leads to a higher depreciation rate and expense than what would have resulted if his estimates had been "based solely on mathematical best fit curves," as witness Spanos claims. (Tr. p. 1055.4-6.)

Mr. Garrett also addressed Witness Spanos' claims that his approach to estimating service lives is at odds with the NARUC depreciation manual because of his emphasis on mathematical curve fitting. He agreed that if a depreciation analyst simply selected the best mathematically

fitting Iowa curve for each account without question, it would run the risk of being at odds with the preferred analytical approach described in the NARUC manual and other authoritative texts in the industry. However, he stated that he is not taking such an approach. Instead, he stated, his approach uses a combination of visual and mathematical curve fitting technique along with professional judgment, in conformance with authoritative depreciation texts, including the NARUC manual. (Tr. p. 1055.6-7.)

He did note, however, that it is fair to say that he relies more on objective analysis than does witness Spanos, and he opined that when the Commission is presented with two service life proposals for a particular account, it should select the curve that is supported more by the objective evidence. (Tr. p. 1055.7-8.)

In surrebuttal, Mr. Garrett also addressed his net salvage proposals. He noted that the Company's currently approved net salvage rates are zero, and he generally agreed with witness Spanos that some level of negative net salvage should be considered in calculating the Company's depreciation rates. However, he stated that large increases in negative net salvage in any given cases are generally not preferable because it can result in a substantial increase in rates to customers, sometimes known as "rate shock." Thus he took issue with witness Spanos' proposal to increase negative net salvage rates by 20%. He also relied on the fact that historical net salvage data was not available for the Company. He opined that the net salvage rate adjustments presented in his testimony strike a fair balance between a complete disallowance of net salvage and the significant increases in negative net salvage proposed by witness Spanos. He stated that as Blue Granite accumulates net salvage data over time, that data can be used to develop accurate net salvage estimates. (Tr. p. 1055.8-9.)

**Company Response**

In rebuttal testimony, Mr. Spanos noted that ORS witness Garrett proposes a fairly significant change in depreciation expense compared to the Company's depreciation studies, due in large part to the changes to service lives he is proposing. Another factor contributing to the decreased expense proposed by Mr. Garrett is that he changes the Company recommended net salvage percentages. (Tr. p. 538.3.)

He stated that a large amount of Mr. Garrett's proposed reduction in depreciation expense is due to Mr. Garrett proposing longer service lives for both water and wastewater plant accounts. Mr. Spanos testified that Mr. Garrett's proposed service life estimates are determined using life analysis that is objectively based solely on mathematical best fit curves without making appropriate determinations and judgments as to which data points should be emphasized. Mr. Spanos emphasized, in contrast, that there must also be a subjective component to life analysis, utilizing expert judgment. (Tr. p. 538.11-21.)

Regarding Mr. Garrett's net salvage estimates for this case, and his claim that the Company proposed estimates are excessive, Mr. Spanos testified that Mr. Garrett had supported as negative or more negative net salvage estimates in a recent case for a majority of the accounts for which he is proposing net salvage changes in this case. (Tr. p. 538.6-9.)

Mr. Spanos emphasized that the depreciation rates proposed in his depreciation study are not excessive. For example, he noted, the net salvage estimates he has proposed are, generally, less negative than those used by most water companies. Additionally, he noted, his proposed depreciation rates were developed using a consistent, systematic and rational approach to



estimating both service lives and net salvage. In contrast, he characterized Mr. Garrett's approach to selecting survivor curves as inconsistent and results-based. (Tr. p. 538.4-5.)

With regard to the selection of survivor curves, Mr. Spanos explained that a highly regarded depreciation text written by Wolf and Fitch states that: "The results of mathematical curve fitting serve as a guide for the analyst and speed the visual fitting process. But the results of the mathematical fitting should be checked visually, and the final determination of the best fit be made by the analyst." He stated that for a majority of the accounts for which Mr. Garrett proposes a different survivor curve, however, his reasons are purely based on a mathematical approach and he does not consider visual curve fitting in his recommendation. (Tr. p. 538.4-5.)

In addition, Mr. Spanos emphasized that it should be expected that there would be an increase in depreciation rates in this case. He stated that Blue Granite is currently depreciating all assets (other than Transportation Equipment) at a rate of 1.5%. This 1.5% rate was first established in 1994 and was subsequently approved in 2005. He concluded that it should come as no surprise that an increase in depreciation expense is warranted in this case. He stated that a 1.5% depreciation rate amongst all plant accounts is significantly lower than what would generally be expected for these types of assets. Additionally, he stated that the 1.5% depreciation rate was developed absent net salvage, meaning it was based on a composite average service life of approximately 66.67 years for all assets. Mr. Spanos observed that Mr. Garrett does not disagree that this is a longer average service life than is to be expected from both water and wastewater plant accounts given that he has only proposed a longer life than 66.67 for two accounts in his testimony. He noted that many accounts have estimated average service lives that are significantly shorter than the 66.67 average service life upon which the current composite depreciation rate is based. Absent net

salvage, he stated, an updated analysis of service lives alone would increase depreciation rates and would do so significantly for some accounts. (Tr. p. 538.5-6.)

Further, Mr. Spanos observed that Mr. Garrett does not disagree that there should be a net salvage component to depreciation rates, as it is expected that there will be costs associated with removing utility assets from service. He stated that when a net salvage component is added to the depreciation rates it will generally increase the depreciation rates even further than the updated service life estimates. Given these factors, he concluded, it should be clear why the increase proposed by Blue Granite and the depreciation study are warranted. (Tr. p. 538.7-8.)

### **Commission Findings**

Depreciation expense allows a company to recover its capital investments in a timely and equitable fashion over the estimated service lives of the investments. Depreciation studies rely not only on statistical analysis but also on the judgment and expertise of the preparer. The Commission recognizes that the determination of depreciation accrual rates requires both statistical analysis and the application of the preparer's judgment and expertise. Because by their very nature depreciation studies rely on examining historic performance to assess future events, a degree of subjectivity is inevitable. The Commission does not consider any one factor in isolation when reviewing the appropriateness of proposed depreciation accrual rates; information gleaned from site visits, information regarding underlying assets in an account, statistical analyses, mathematical and visual curve fitting, and expert judgement are examples of some of the myriad factors the Commission finds relevant in evaluating proposed depreciation rates.

The evidence is clear in this case that an update to Blue Granite's depreciation rates and depreciation expense is needed; both Mr. Spanos and Mr. Garrett are in agreement on this. The

evidence shows that the Company's current depreciation rates are artificially low and out of date. The question is whether Mr. Spanos or Mr. Garrett's proposed accrual rates and expense level are more reasonable and supported by substantial evidence.

Mr. Spanos' proposed accrual rates are based on a combination of historical information, information gathered on site visits, statistical analyses, mathematical and visual curve fitting, and extensive expert judgment. Mr. Garrett's proposed accrual rates are based largely on mechanistic and mathematical approach, ignoring in many cases visual curve fitting techniques, and lacking information from site visits and extensive expert judgment such as that possessed by Mr. Spanos. We also note that Mr. Spanos' net salvage estimates are somewhat conservative in this case, as they are less negative than those used by most water companies.

In this case, we find that Mr. Spanos' proposed service lives and net salvage estimates are the most reasonable and should be approved. Our finding is based upon his expertise in the field, including his expertise with water and wastewater depreciation studies; his presentation of his depreciation studies and the rationales therefor; and his approach of combining mathematical calculations with the application of expert professional judgment and visual curve fitting techniques.

### **iii. Non-Revenue Water**

As discussed in more detail below, we direct the Company to conduct leak testing on the four systems for which leak testing is economical, and to contract with a third party to have a water audit conducted. We will permit Blue Granite to recover its third party purchased water and sewer treatment expenses, except that such recovery shall exclude non-revenue water amounts over 20 percent for the four systems for which leak detection is economical.

**Blue Granite's Position**

Blue Granite opposes ORS's proposed disallowance of recovery for non-revenue water amounts of greater than 10 percent. Blue Granite points out that the 1996 American Water Works Association ("AWWA") committee report on which ORS relies has been rejected by the AWWA, which now favors a more tailored, system-specific approach. (Tr. p. 363.3-4.) Quoting a 2019 report from the AWWA, Blue Granite states that, "[s]ince 2003, AWWA has recommended that it is best for utilities to set system-specific loss targets, and not use a prescribed one-size-fits-all number." (Tr. p. 363.4 (quoting *Key Performance Indicators for Non-Revenue Water*, AWWA Water Loss Control Committee Report (Nov. 2019), available at <https://www.awwa.org/Portals/0/AWWA/ETS/Resources/WLCKPIReport%202019.pdf?ver=2019-11-20-094638-933>)).

Blue Granite also points out that 5 of the systems listed by ORS were served by Company wells during the 12-month period utilized, and therefore it is not determinable whether water losses are generated from the source wells or the purchased supply connection (Tr. p. 363.5).

Blue Granite states that it is taking proactive steps to reduce non-revenue water consistent with AWWA recommendations, and should not be penalized by utilizing an arbitrary threshold that the AWWA has explicitly rejected. The Company proposes an evaluation based on benefit-cost analysis consistent with AWWA's recommendations, including setting goals for each system and to evaluate the Company's efforts towards reducing non-revenue water for each. (Tr. p. 363.8.) Blue Granite accepts ORS's recommendation to engage a third-party to complete water audits for its systems, and requests the Commission authorize deferral treatment of these costs, and accrual of carrying costs, to facilitate recovery in the Company's next rate case. (Tr. p. 363.8.)

Should the Commission deem a particular threshold is warranted in this proceeding, Blue Granite would propose a 20% threshold based on the ongoing efforts of the Company, the costs required to reduce non-revenue water, and the standards used by other jurisdictions. (Tr. p. 363.9-10.)

### **ORS's Position**

ORS proposes a disallowance for all non-revenue water of greater than 10 percent on the basis that it “insulates the ratepayers from non-revenue water impacts and incentivizes the Company to monitor and mitigate non-revenue water,” and states that it is consistent with the AWWA’s benchmark for non-revenue water as articulated in a 1996 committee report. (Tr. p. 1201.5.)

### **Commission's Finding**

On some systems, the cost of leak testing would exceed—and, in some cases, greatly exceed—the cost of non-revenue water. These costs would be part of the Company’s cost of service and would be passed along to customers. For that reason, disallowing the Company’s recovery of non-revenue water in cases where it is not economical to invest would incentivize the Company to make uneconomic investments, which would actually **drive up** costs for ratepayers rather than insulate them. At the merits hearing, while ORS Witness Maurer agreed that the costs of addressing non-revenue water must be weighed against the resulting benefits and that customers would bear the costs of conducting a water audit—Tr. p. 1250, lines 15-24—the costs of leak detection and a water audit (which could occur on an annual basis) could be exceedingly more than the cost of non-revenue water. (Tr. p. 1249). Additionally, the water audit and leak detection process would not “fix the problem”; follow-on infrastructure repairs and replacements would be necessary and may only result in a partial mitigation of losses. (Tr. p. 1249-50.)

It is uncontested that customers would be required to pay for any investment associated with mitigating non-revenue water, to include leak detection and any resulting infrastructure repairs or replacements. It would be unreasonable for this Commission to require customers to pay large sums for leak detection in cases where the related costs would exceed the non-revenue water costs. For that reason, for the four systems for which leak detection would actually be economical—Peachtree Acres, I-20, Hidden Lakes, and Hill and Dale—we direct that the Company begin leak testing and associated repairs within 12 months of this order. We will, moreover, disallow recovery of purchased water expenses for these four systems above the 20 percent non-revenue water level. While the AWWA has rejected a universal threshold for non-revenue water, we find that this blended approach—detecting and repairing leaks on problematic systems and disallowing recovery of excessive non-revenue water on those systems—strikes a rational and reasonable balance between incentivizing the utility to invest in its system while not being overly punitive against the utility, or requiring customers to bear costs when the investment is not economical.

The Company is further directed to contract with a third party for the purpose of conducting a water audit for its purchased water systems. Because these leak testing and water audit costs are unusual or extraordinary in nature, and because of their anticipated potential magnitude, the Company is authorized to defer the associated expenses into a regulatory asset account, and accrue carrying costs at the Company's authorized cost of debt until the time of recovery.

**iv. Pass-Through Mechanism for Purchased Services**

We find that the pass-through mechanism, as modified as described below, is a reasonable proposal that is in the best interests of both customers and the Company.

**Blue Granite's Proposal**

Blue Granite proposes to implement a mechanism by which its rates for recovery of purchased water and sewer treatment expenses would be updated on an annual basis to reflect increases or decreases in third-party service provider rates. Application ¶ 19. The changes in such rates would be isolated within a standalone “Purchased Sewer Treatment Adjustment Charge” and a standalone “Purchased Water Adjustment Charge,” and the annual rate adjustment for purchased water expense deferrals and annualized vendor rate changes would be applied to “Distribution only” customers, and purchased sewer treatment deferrals would be applied to “Collection only” customers. (Tr. p. 764.37.)

Under the proposed mechanism as described in the Application, changes in expenses would be deferred, and the Company would file for a rate adjustment within 60 days of the end of each annual deferral period. The ORS and the Commission would then review and audit the filing within 45 days thereafter, and the Company would notify its customers of the audited rate adjustment within 15 days of audit completion, with the approved rate would become effective 30 days thereafter. The interim adjustment rates would be reset to zero in the next base rate case as the vendor rate changes and deferred expenses are incorporated into the setting of base rates. Application ¶ 19.

In testimony, Blue Granite noted—and we take judicial notice of the fact—that no other water or wastewater utility with a pass-through mechanism provides the opportunity for a hearing as part of their mechanism. (Tr. p. 763.39.) The Company also explained that the mechanism is intended to reduce regulatory costs for customers and to free up Commission resources, and that it believed there would be little to gain from a hearing on a mechanism that simply passes through

third party costs. In spite of these reservations, the Company expressed a willingness to including the opportunity for a hearing as part of its annual mechanism proceeding. (Tr. p. 763.39.)

In response to ORS's argument that the pass-through mechanism should "de-consolidate" rates and instead pass through third-party expenses on a localized basis, the Company offered testimony that such a position is counter to a policy favoring greater consolidation of Blue Granite's rates. The Company also offered testimony that the Bonbright principles, often referred to in a regulatory context, strongly support implementation of the pass-through mechanism. (Tr. p. 764.8.) In particular, the Bonbright principles support: (1) the ability of the utility to earn its permitted revenue requirement without expanding rate base; (2) revenue stability and predictability through a once-annual rate adjustment; (3) rate stability and predictability through a once-annual rate adjustment, rather than a less frequent rate change that could result in rate shock or a more frequent rate change that could result in whiplash and customer confusion; (4) the reflection of all costs of service in rates by more prompt updates to the rate; and (5) a mechanism that tracks changes in rates on a dollar-for-dollar basis, and therefore tracks changes in supply patterns. (Tr. p. 764.8-9.)

In rebuttal testimony, Company witness DeStefano also pointed out that the ORS' position (discussed below) is inherently contradictory. The ORS proposes that rate consolidation should continue, but these third-party costs should be recovered on a non-consolidated basis; the ORS proposes that these third-party costs should continue to be deferred and recovered from customers in subsequent rate cases on a consolidated basis, but the ORS objects to the pass-through mechanism on the basis that recovery will take place on a consolidated basis. Tr. p. 764.6-764.7.

#### **The Consumer Advocate's Position**



The Consumer Advocate supports Blue Granite's proposed pass-through mechanism. The Consumer Advocate offered the following testimony:

Consolidated rates are an overall benefit for customers as they create economies of scale and lowers administrative and regulatory costs to all customers. In this instance, customers benefit, especially those on smaller systems, because the cost of providing safe and reliable service is minimized.

Also, I believe an annual rate filing to pass-through changes in the cost of purchased water and wastewater service will minimize the effect on BGWC's overall rates it charges for current water and wastewater services. In other words, if the current deferred accounting system, which accumulates the costs related to changes in the supplier rates for purchased water and wastewater services, continues, then there is likely to be large balances that will need to be recovered in every rate case. For instance, in this proceeding, the Company is seeking recovery of \$2.8 million of purchased water and wastewater costs that have been deferred. Annual rate filings will prevent the accumulation of such balances. To the extent there are any increases in the rates purchased water and wastewater suppliers charge, those increases will be pass-through in smaller increments that are more palatable to customers.

(Tr. p. 658.10). Consumer Advocate Witness Morgan also offered testimony at the merits hearing that the pass-through mechanism is not unreasonable and is in customers' interests because it supports gradualism in rates. The only concern he expressed was related to the non-revenue water issue, which we address in this Order. (Tr. p. 708.)

### **ORS's Position**

ORS opposes the mechanism because—as originally proposed—it did not allow for public participation in the proceeding, though ORS acknowledges that the Company has clarified that it would be open to providing for the opportunity of a hearing. (Tr. p. 1213.21-22.) ORS recommends that the Company be permitted to continue deferring its third-party water and sewer treatment costs and recover these costs in the next base rate proceeding. (Tr. p. 1213.23.) ORS also opposes the pass-through mechanism as proposed by the Company because it does not account for non-revenue

water or inflow and infiltration. ORS notes that it “has proposed an adjustment to the Company’s purchased water deferral and purchased water expenses in this proceeding based on its review of the Company’s purchased water expense and management practices.” (Tr. p. 1214.3-4.)

During the merits hearing, ORS agreed that the Company’s deferred increases in third party expenses would be recovered on a consolidated basis, which conflicts with ORS’s position that these expenses be recovered on a localized basis. ORS also agreed that it supports further rate consolidation for Blue Granite. (Tr. p. 1225-29.)

### **York County’s Position**

York County asserts that Blue Granite’s consolidated rate structure as implemented through the pass-through mechanism will disproportionately affect York County customers because the County has suspended its previously approved rate increases.

### **Commission’s Finding**

We find that the pass-through mechanism, with certain limited modifications, is a reasonable method by which Blue Granite can be made whole for its necessary third-party purchased water and sewer treatment service expenses. We find that the pass-through mechanism benefits customers by regularly and predictably adjusting rates based on periodic changes—including increases **and** decreases—in third-party service providers’ rates. Nevertheless, as discussed above, we believe that a reasonable limit on non-revenue water is appropriate. Therefore, in addition to the water audit ordered above, which should reduce non-revenue water in the long-term, we also will require Blue Granite to exclude from its annual pass-through calculations the recovery of purchased water expenses for the Peachtree Acres, I-20, Hidden Lakes, and Hill and Dale systems above the 20 percent non-revenue water level. These are the

four systems for which leak testing would be economical. We reiterate that disallowing the Company's recovery of purchased water expenses on systems for which the associated investment would be uneconomical would require customers to bear costs of leak detection and repairs when such investment is not economical. This cost-benefit analysis can and should be updated on a system-by-system basis at the Company's next base rate proceeding.

We agree that the pass-through mechanism should utilize the same consolidated rate design of the Company's existing rates – i.e., Water Service Territories 1 and 2, and Consolidated Sewer. As described in the Consumer Advocate's testimony, we have long favored a consolidated rate design, as such represents an overall benefit for customers, creating economies of scale and lowering administrative and regulatory costs for all customers. (Tr. p. 658.9.) Further, customers benefit, especially those on smaller systems, because the cost of providing safe and reliable service is minimized. Whether a particular geographic area would benefit over another in the short term is inapposite to these considerations.

Similar to cost recovery mechanisms approved for energy efficiency and demand-side management programs—*see, e.g.*, Order No. 2015-596 at 10-12, Docket No. 2015-163-E (Aug. 19, 2015)—we approve the following procedure for the Company's annual pass-through mechanism:

- Beginning in Blue Granite's 2021 pass-through proceeding, the Company's rate adjustment period will include any changes in third-party rates occurring between that which is captured in this rate proceeding through December 31, 2020. Thereafter, the rate adjustment period will be the preceding full calendar year.

- On or before December 15<sup>th</sup> of each year, the Commission’s Clerk’s office will issue a notice to be provided to customers of the following pass-through proceeding and associated deadlines.<sup>1</sup> See Order Exhibit No. 1 for a sample Notice of Proceeding.
- On or before March 1<sup>st</sup> of each year, Blue Granite will file its annual pass-through application in the instant docket, Docket No. 2019-290-WS, and serve it upon the parties to this proceeding.
- On or before April 15<sup>th</sup> of each year, the ORS and any interested parties may file comments on the Company’s application. In such comments, parties may request a hearing. While the calculation of changes in third party rates is strictly a mathematical exercise, to the extent there is an evidentiary dispute that can only be resolved through a hearing, such a request for hearing will be considered.
- On or before June 1<sup>st</sup> of each year, the Commission will rule on the Company’s annual application. The Company will implement the authorized rates effective on the date of Commission approval.

Inasmuch as we are approving the pass-through mechanism in this proceeding, we will permit the Company to recover the costs associated with the notice and filing costs associated with the annual pass-through proceeding, as accounted for in Adjustment Nos. 15b and 16b. In addition, we authorize the Company to defer its pass-through expense increases and decreases incurred from

---

<sup>1</sup> We note that such “pre-notice” is consistent with that used in utilities’ annual fuel filings, whereby notice of the proceeding is provided to customers ahead of the utility’s filing. See, e.g., Notice of Hearing and Prefile Testimony Deadlines, Docket No. 2020-1-E (Dec. 9, 2019).

its vendors on an interim basis, as necessary until such changes are reflected in rates through the pass-through mechanism.

**v. Deferred Maintenance Expenses**

As discussed below, we find that the Company's demonstrated investment in multi-year maintenance activities should be normalized and amortized over the period for which the benefit will be realized, and such upfront investment, net of amortization incurred, shall be included in rate base so as to compensate the Company for the time value of its investment.

**Company Proposal**

Mr. DeStefano testified that deferred maintenance expense was adjusted to reflect amortization of systemwide hydrotank inspections which occurred after the end of the Test Year (as well as to remove Test Year activity for items now fully amortized). (Tr. p. 763.12.)

In rebuttal testimony, the Company agreed to the update to actual deferred maintenance costs made by ORS in Adjustment No. 9a. However, Company witness DeStefano testified that it is appropriate to defer the maintenance costs and include the unamortized balance of the deferred tank inspections in rate base. He stated that such maintenance costs, similar to tank painting, are significant and do not recur on an annual basis. He testified that they provide a multi-year benefit to the Company and its customers. He noted that in the case of tank inspections, they are performed every five years, and tank painting value can last approximately 20 years. He stated that this multi-year benefit is reflected first in the form of a deferral and amortization, but as the Company is funding the costs upfront for a benefit derived over multiple years, the amount is analogous to a prepaid item and therefore appropriately included in rate base. In any event, Mr. DeStefano

testified, these important but periodic maintenance costs should be included in rates and recovered over a reasonable period of time. (Tr. p. 764.26-27.)

### **Consumer Advocate Position**

Consumer Advocate Witness Morgan opposes the deferral of the hydrotank inspection costs and recommends removing the unamortized deferred maintenance balance from rate base, under the rationale that these are simply routine maintenance costs. In surrebuttal testimony, Mr. Morgan stated that these costs are not eligible for capitalization under GAAP. He added that, even when regulatory commissions allow recovery of such deferred maintenance costs, they normalize such costs over a reasonable period of time rather than including them in rate base. (Tr. 651.12, 658.7-8.)

### **ORS Position**

ORS Witness Sullivan proposed adjusting the Company's filing position to account for the actual deferred maintenance costs incurred for system-wide hydrotank inspections in the post-Test Year period, and recommended recovery of the actual costs over a 5-year amortization period. Witness Sullivan also recommended removing the unamortized deferred maintenance balance from rate base. In surrebuttal testimony, Mr. Sullivan reiterated that these expenses are maintenance expenses not capital investments, with the former traditionally not reflected in rate base. Additionally, he testified that ORS's exclusion of these expenses from rate base is consistent with Commission precedent. (Tr. p. 1115.21, 1116.4-6.)

### **Commission Findings**

No party disputed that hydrotank inspections were necessary, nor did any party dispute the costs of such inspections. Rather, the dispute among the parties centers around whether such costs

should be reflected in rates in this proceeding and, if so, the proper ratemaking treatment for such costs, that is, rate base or expense treatment. We find that such costs should be reflected in rates. Hydrotank inspections are a reasonable and necessary part of providing water utility service, and the fact that inspections do not occur each and every year does not mean that a reasonable, normalized amount of tank inspection costs should be excluded from the ratemaking process. Accordingly, we reject the Consumer Advocate's recommendation.

Additionally, we agree with the Company that hydrotank inspection costs are effectively an upfront investment by the utility that benefits customers and supports capital investments made by the Company, even though the costs of such are recovered ratably over a period of years. The recovery of the dollar-for-dollar investment over multiple years does not fully compensate the Company for the upfront investment's impact, and therefore such costs that result in a multi-year benefit should generate a return, which is not otherwise accounted for in the revenue requirement. For this reason, we find it is appropriate to defer the maintenance costs and include the unamortized balance of the deferred tank inspections in the Company's rate base. Accordingly, we reject the ORS's proposal to reflect such costs as an O&M expense rather than as a rate base item.

**vi. Amortization of Deferral Balances**

As discussed below, we find that the amortization period for the decommissioning of the Stonegate water treatment plant ("WTP") and Friarsgate wastewater treatment plant ("WWTP") should be matched to the remaining lives of the actual retired assets. We also find that the deferral balances for hurricane costs, I-20 Phase 2, Stonegate decommissioning and net book value ("NBV"), Friarsgate decommissioning and net book value, and EDIT reserves should be calculated to 4/30/2020, because there are no known or measurable changes to the balances that will occur

after that time, and any date beyond this point is inconsistent with the historical test year approach utilized by the Commission in setting rates.

**Company Proposal**

Mr. DeStefano testified that, pursuant to Commission Order No. 2018-182, the Company has been deferring litigation expenses related to two cases before the Administrative Law Court – the DHEC Permit Denial case and the I-20 Interconnection case. He stated that the Company requests recovery of the related deferred costs of \$216,773 and \$65,948, respectively, in this case, over a five-year period. He confirmed that these proceedings have concluded as of the time of his testimony. (Tr. p. 763.9-10.) In addition, Mr. DeStefano testified that, pursuant to Commission Order No. 2018-308, Blue Granite has deferred the revenue impact of the difference between a 35% federal income tax rate and the 21% federal income tax rate per the TCJA, for the period of January 1, 2018 through June 29, 2018, the date of the 2017 rate case's change in customer rates. He stated that the Company proposes to refund this deferred liability \$335,713 to active customers at the time of the Order issued in this case, through a one-time credit of \$10.64 to each customer water and wastewater service account – that is, a customer served both water and sewer would receive a one-time credit of \$21.28. (Tr. p. 763.10.)

Mr. DeStefano also testified that the Company included in its revenue requirement the removal costs to decommission the Stonegate WTP and net book value of the related assets for a combined deferral of \$756,503, to be amortized over a 19.82 year period. He stated that the Company also included in its revenue requirement the removal costs to decommission the Friarsgate WWTP and net book value of the related assets for a combined deferral of \$7,006,490, to be amortized over a 19.72 year period. He explained that these amortization periods are derived



based on the weighted average of the remaining lives of the WTP and WWTP assets removed from service. The Company also requested authority to defer for subsequent recovery, capital costs associated with decommissioned plant assets including costs of removal and remaining net book value. (Tr. p. 763.10, 15.)

Finally, Mr. Destefano testified that the Company updated its Excess Deferred Income Tax (“EDIT”) balances – generated from the remeasurement of Accumulated Deferred Income Taxes (“ADIT”) based on the TCJA’s change in federal income tax rate from 35% to 21% - due to the filing of its final 2017 federal tax return after the inclusion of the EDIT reserve and amortization in its 2017 Rate Case. He stated that the updated EDIT reserve balance for protected assets is \$2,742,706 and for unprotected assets is \$111,437 as of December 31, 2019. (Tr. p. 763.10-11.)

In rebuttal testimony, Mr. DeStefano testified in opposition to the ORS’ proposed longer amortization periods for the decommissioned plant and associated remaining net book value of the removed assets. He noted the illogic of tying the amortization period to a new replacement asset rather than to the decommissioned assets that are the basis for the remaining costs. He also noted that the fact that the Company’s depreciation rates have been very low for many years necessarily resulted in assets at the end of their useful life but with a net book value remaining. He testified that, effectively, customers have received the benefit of the full life of these assets but the Company’s recovery was prescribed over a longer presumed asset life, and therefore the Company has under-recovered the cost of the assets. He stated that utilizing a longer period than is reflected in the Company’s calculation—which uses Witness Spanos’s proposed depreciation rates, correcting for past under-depreciation—would result in unreasonably extending the period of under-recovery for the Company of these now-retired assets. Rather, he testified, the Company’s

proposed remaining life calculation for amortizing the decommissioning and NBV asset amounts rectifies this issue of under-depreciation to date. (Tr. p. 764.29-30.)

Mr. DeStefano also indicated in his rebuttal testimony that the Company agrees with ORS Witness Briseno's calculations of the deferral balances for hurricane costs, I-20 Phase 2, Stonegate decommissioning and net book value, Friarsgate decommissioning and net book value, and EDIT reserves to 4/30/2020. However, he testified, the Company disagreed with ORS's calculation of the decommissioning/NBV and EDIT balances through 4/30/2021, a full 22 months beyond the Test Year-end and over 16 months past the audit cut-off date. Instead, Mr. DeStefano testified, the Company recommends all deferral balances be calculated as of the same cut-off date of 4/30/2020, as there is no foreseeable change in the amortizable balance that will occur between the audit cut-off and this date, which reflects the day before rates are estimated to be effective in this case. (Tr. p. 764.30, 764.35-36.)

### **ORS Position**

Although the ORS updated some of the deferred amounts, the ORS did not object to the Company's proposed amortization periods except with respect to the Company's decommissioned plant and associated remaining net book value of the removed assets and the EDIT balances. For the decommissioned plant and associated remaining net book value deferrals, the ORS recommended longer amortization periods based on the estimated useful lives of the new, replacement interconnect project. The ORS also proposed that the decommissioning/NBV and EDIT balances be calculated through 4/30/2021. In addition, the ORS updated the one-time customer credit resulting from the TCJA regulatory liability, to \$10.59 per account. (Tr. p. 1128.6-7, 1213.12-13, 1129.2-4, 1214.9-11.)

**Commission Findings**

The parties appear to be in agreement on the amounts and amortization periods for litigation expenses and the TCJA regulatory liability and one-time customer account credit, and we approve such amounts and amortization periods. In addition, there appears to be no objection to the Company's request for authority to defer for subsequent recovery, capital costs associated with decommissioned plant assets including costs of removal and remaining net book value, and we so authorize the Company to defer such costs.

In dispute is the appropriate amortization period for the remaining net book value for decommissioned assets—assets that have been used and useful in providing service to customers for years. The Company has proposed that the costs of removal and remaining net book value associated with the decommissioned assets be amortized over slightly less than 20 years, based on the weighted average of the remaining lives of the WTP and WWTP assets removed from service. The ORS, on the other hand, proposes longer amortization periods for these costs tied to the estimated service lives of the new, replacement assets. We fail to see the logic of tying the amortization periods for old, retired assets to the estimated lives of the new, replacement assets, as opposed to basing the amortization periods on the remaining lives of the actual assets that were decommissioned. In addition, we find persuasive Mr. DeStefano's testimony that customers have received the benefit of the full life of these assets, while the Company's recovery of such asset costs was calculated on an artificially longer estimated asset life, due to the Company's low depreciation rates. The Company's proposal reasonably minimizes intergenerational inequity, while the ORS's proposal would exacerbate it. Accordingly, we find the Company's proposed

amortization periods for its costs of removal and remaining net book value associated with decommissioned assets to be reasonable, and we approve the use of such amortization periods.

The parties also appear to be in agreement with respect to the ORS's calculations of the deferral balances for hurricane costs, I-20 Phase 2, Stonegate decommissioning and net book value, Friarsgate decommissioning and NBV, and EDIT reserves to 4/30/2020. However, the Company disagrees with ORS's calculation of the decommissioning/NBV and EDIT balances through 4/30/2021. As Mr. DeStefano stated, that is a full 22 months beyond the Test Year-end and over 16 months past the audit cut-off date. We agree with the Company that all deferral balances be calculated as of the same cut-off date of 4/30/2020, as there is no evidence of foreseeable changes in the amortizable balance that will occur between the audit cut-off and this date, which approximates the timing of rates to be effective in this case. Carrying the amortization of these deferral balances beyond this point would result in recognizing impacts to rate base into the rate effective period, which would be inconsistent with the historic test year basis upon which rates are normally set by the Commission. Accordingly, we find that all deferral balances shall be calculated as of 4/30/2020 for purposes of this case.

**vii. Accumulated Depreciation and Accumulated Amortization of CIAC**

As discussed below, we agree with the Company that Accumulated Depreciation and CIAC amortization balances should not be updated for future depreciation rates that are not in effect at the time of the rate base cut-off date

**ORS Position**

The ORS proposed updating test year accumulated depreciation and CIAC amortization (see Adjustment Nos. 33 and 36). Specifically, in Adjustment No. 33, item 4, ORS Witness Briseno

proposes to adjust accumulated depreciation for the depreciation expense calculated using ORS Witness Garrett's proposed depreciation rates applied to ORS's calculation of gross plant in-service. In Adjustment No. 36, ORS proposes an adjustment to CIAC to reflect the amortization of CIAC expenses, pro forma CIAC additions and decommissioned plants, using ORS Witness Garrett's proposed depreciation rates and updates to CIAC provided by the Company on the audit cut-off date (December 20, 2019). (Tr. p. 1128.12-13.)

### **Company Response**

Blue Granite Witness DeStefano testified that the Company disagrees with the calculation and application of Item 4 of Adjustment No. 33 and with Adjustment No. 36, sponsored by ORS Witness Briseno. Mr. DeStefano testified that it appears that ORS has applied a depreciation adjustment to Accumulated Depreciation and an amortization adjustment to Accumulated Amortization that utilizes future, *proposed* depreciation/amortization rates, which would not be in effect until after issuance of the Commission's Order, well after the audit cutoff of December 20, 2019. He stated that incorporating the effects of post-audit cutoff changes for only certain components of rate base, without the ability to similarly account for the effects of inter-related activity in Utility Plant in Service and CIAC (*i.e.*, capital and CIAC additions after 12/20/2019), creates a violation of the matching principle prioritized in utility regulation.

Instead of this approach, Mr. DeStefano recommended that the Commission approve a rate base balance with the balances of its components utilizing a consistent cutoff period for interrelated components, in this case Utility Plant in Service with Accumulated Depreciation and CIAC with Accumulated Amortization. Likewise, he stated, such rate base balances should not include the impacts of prospective depreciation and amortization rates that were not in effect during the post-

Test Year period before an Order in the current proceeding is effective. He stated that utilizing prospective activity in determining the actual, supported rate base balances goes beyond the historic Test Year basis for setting rates utilized by the Commission. For that reason, he emphasized that a single cut-off date should be used for inter-related rate base items to apply consistent, matching treatment to each item. (Tr. p. 764.34-36.)

Mr. DeStefano observed that, while the general matching principle identified above is relevant for Utility Plant in Service and CIAC, it is less of a consideration for deferral balances in rate base. This is because, while Utility Plant in Service and CIAC balances (and therefore, the fully dependent Accumulated Depreciation and Amortization balances) change regularly due to constant activity related to the Company's infrastructure after the audit cut-off date, deferral balances are discrete, unchanging original balances that, once approved, have no further variables that affect their rate base consideration. He stated this makes the deferral balances and their related amortization "known and measurable" in a complete sense, consistent with traditional ratemaking principles, which differentiates them from Utility Plant in Service and CIAC and their related Accumulated Depreciation and Amortization balances. For this reason, he explained, the Company has accepted ORS's adjustment of the unamortized balances for certain prior-approved deferrals – hurricane costs, I-20 Phase 2, purchased water/sewer treatment deferrals – as carried out to 4/30/2020, but rejects ORS's calculation of the decommissioning/net book value and EDIT balances through 4/30/2021. (Tr. p. 764.34-36.)

### **Commission Findings**

We agree that Accumulated Depreciation and CIAC Amortization balances should not be updated for future depreciation rates that are not in effect at the time of the rate base cut-off date.

Mr. DeStefano is correct that adopting ORS's position would violate the matching principle by effectively mixing pre-Order balances with post-Order effects, such as new depreciation rates. Similar to the cut-off for deferral balances of 4/30/2020 as described above in this Order, incorporating activity beyond that which is historically supported and directly measurable results in rates that on Day 1 of their effective period would discount the true balances that were supported in the rate case. Additions and retirements to gross plant in-service and CIAC occur on a regular basis, and, as such, extrapolating the fully dependent Accumulated Depreciation and Amortization balances does not constitute a known and measurable activity. Further, by carrying Accumulated Depreciation and CIAC Amortization balances a full year into the rate effective period as proposed by ORS, the Company will never recoup over twelve months of investment in its infrastructure, nor the return on that balance. As a result, it would not have a reasonable opportunity to earn its authorized return. *See Southern Bell*, 270 S.C. 590 at 607-08 (1978) ("The rates established by a utility regulatory commission must not only provide the utility with the opportunity of recovering its reasonable operating expenses, but must also provide a fair and reasonable return on the investments made by the company in providing utility service to its customers.").

Accordingly, we find that a single cut-off date should be used for inter-related rate base items to apply consistent, matching treatment to each item – in this case, the December 20, 2019 cut-off date.

#### **viii. Storm Recovery Expense**

As discussed in more detail below, we will set the Company's Storm Recovery Expense using a five-year average, as such is more reflective of recent conditions and costs incurred.

#### **Blue Granite's Proposal**

For Storm Recovery Expense, Blue Granite had initially proposed an amount of \$51,802 based upon storm-related expenses experienced during the historic test year. (Tr. p. 763.22, 1190.15.) In response to ORS’s position that storm expense should be based on a normalized multi-year average, the Company proposed to use an average of the last 5 years (2015-2019) of storm recovery expenses, which is \$42,494. (Tr. p. 764.21-22.) The Company stated that a more recent average than that used by ORS because South Carolina has experienced more severe storms in recent years, and as a result, the Company has experienced consistently higher levels of storm recovery costs in recent years. *Id.* The Company included the following table of annual storm expenses in its testimony, which removes costs requested and authorized for deferral from Hurricanes Joaquin, Florence and Michael, the contents of which no party contested:

Year	Storm Costs	Five-Year Average
2010	\$16,207.41	\$14,533.90
2011	\$31,631.02	
2012	\$1,510.19	
2013	\$4,942.69	
2014	\$18,378.21	
2015	\$47,938.40	\$42,493.62
2016	\$43,737.13	
2017	\$33,469.27	
2018	\$54,716.21	
2019	\$32,607.10	

(Tr. p. 764.22.)

### **ORS’s Position**

ORS recommends a ten-year normalization of storm costs (eliminating the highest and lowest years), because, in its view, that is “a reasonable period of time to form an accurate view of storm costs.” (Tr. p. 1191.8.) At the merits hearing, ORS conceded that its proposed \$28,000



recovery would not cover any one of the previous five years of storm costs, and ORS recognized that the most recent five years had demonstrated an increase in the Company's storm expenses. (Tr. p. 1244-45.)

### **Commission's Findings**

Based on the evidence in the record, we find and conclude that the Company's proposed five-year average, 2015 to 2019, of \$42,493.62 is an appropriate level at which to set the Storm Recovery Expense. The recent trend for the Company's storm costs has been an expense level well above that experienced in prior years. As elucidated during the merits hearing, were we to adopt ORS's recommendation of \$28,320.51, the Company would not have been made whole for storm costs in any one of the previous five years. (*See* Tr. p. 1244.) There is therefore no rational or evidentiary basis for setting the Storm Recovery Expense at that level. We instead adopt the most recent five-year average.

#### **ix. Storm Reserve Fund**

As discussed in more detail below, we will permit Blue Granite to establish a Storm Reserve Fund as originally proposed, to be reevaluated during the Company's next base rate proceeding.

### **Blue Granite's Proposal**

The Company states that a Storm Reserve Fund will facilitate the expeditious repair and recovery of the Company's essential facilities, infrastructure, and services, and will minimize the need for deferred accounting petitions, reducing administrative burden, as well as mitigate the financial impact of such extraordinary costs that are otherwise unable to be considered in the setting of revenue requirement. (Tr. p. 763.20.) Blue Granite states that the \$200,000 funding level

was chosen based on the approximate level of storm recovery costs incurred by the Company in the wake of Hurricane Florence and Hurricane Michael in September/October 2018, which totaled \$208,713. (Tr. p. 763.22.) In rebuttal, the Company states that the \$50,000 funding level proposed by ORS would be insufficient to accomplish the fund’s intended goals. (Tr. p. 764.24.)

### **ORS’s Position**

ORS supports the establishment of a Storm Reserve Fund, but recommends that the fund be limited to \$50,000, which, in its view, “is more closely aligned with the Company’s average annual expenses for storm costs.” (Tr. p. 1190.21-22.) ORS recommends that the fund be utilized for damage incurred by storms named by the World Meteorological Organization, and only if the Company’s insurance does not cover all associated costs. (Tr. p. 1190.21.) ORS proposes that the Company report quarterly to the Commission and ORS the status updates of the fund including, but not limited to, dates and amounts of withdrawals and expenditures from the Fund, current balance, and current monthly surcharge. (Tr. p. 1190.21.)

### **The Consumer Advocate’s Position**

The Consumer Advocate opposes the establishment of a Storm Reserve Fund on the basis that “a significant portion of [Blue Granite’s] infrastructure is below ground.” (Tr. p. 651.19.) The Consumer Advocate also argues that the Company’s storm costs are already included in the cost of service. (Tr. p. 651.20.)

### **Commission’s Finding**

We will permit Blue Granite to establish a Storm Reserve Fund as originally proposed, to be reevaluated during the Company’s next base rate proceeding. We agree that such a fund will facilitate the expeditious repair and recovery of the Company’s essential facilities, infrastructure,

and services, and will minimize the need for deferred accounting petitions, reducing administrative burden, as well as mitigate the financial impact of such extraordinary costs that are otherwise unable to be considered in the setting of revenue requirement based on a single historic test year. (*See* Tr. p. 763.20.) The \$200,000 funding level is roughly equivalent to that recently expended by the Company in response to Hurricanes Florence and Michael in 2018, which was \$208,713, and is sufficiently high to mitigate potential deferred accounting requests should a similar storm impact be incurred. (Tr. p. 763.22.) This fund would work in conjunction with the above authorized \$42,493.62 normalized Storm Recovery Expense level included in base rates, such that it would be utilized for costs incurred above the base rate level of recovery, and should expense levels fall below the base rate level in a 12 month period, the excess base rate recovery would be credited to the reserve fund to benefit customers.

We can reevaluate the utility of the fund in the Company's next base rate proceeding. In response to the Consumer Advocate's concern that Blue Granite's storm costs are already included in rates, we would point out that the Storm Reserve Fund is distinct from and in addition to the Company's more routine storm recovery expenses. (*See* Tr. p. 764.22 ("[T]hese [storm recovery expense] amounts exclude storm costs for Hurricanes Florence and Michael because Blue Granite has separately tracked and deferred those costs."))

**x. Round Up Program and Associated Costs**

As discussed below, we approve the Company's proposal to establish a Round Up program, and—as recommended by the Consumer Advocate—to defer for recovery in its next base rate case its implementation costs associated with the program, up to a cap of \$50,000 for such costs.

**Company's Proposal**

The Company seeks approval to implement a voluntary “Round Up” program under which participating customers’ bills would be “rounded up” to the nearest higher dollar, and the difference being accumulated in a reserve fund. The funds would be remitted to the South Carolina Office for Economic Opportunity (“OEO”) and then distributed by the OEO to Community Action Agencies in the Company’s service territory to assist Blue Granite’s low-income customers with their water and sewer bills. In connection with its request for approval of this program, Blue Granite seeks recovery of \$14,674 for bill inserts and flyers to be used to communicate with customers about this new program (included in the Company’s proposed revenue requirement as a pro forma adjustment). The Company also seeks approval to defer implementation costs for the Round Up program related to modifications of its billing system and MyUtilityConnect customer service application, for recovery in the Company’s next base rate case. Mr. DeStefano’s testimony explained that customers would “opt in” to the program either through the MyUtilityConnect mobile app or by calling the Company’s Customer Service Center. (Tr. p. 763.23-24.)

In its surrebuttal testimony, the Company responded to certain positions of ORS, noting that the program, although voluntary, is part of its service offering and part of its cost to serve customers. Further, although difficult to quantify, the existence of the Round Up Program and the accompanying assistance to lower income customers should result in fewer disconnect/reconnect (and therefore lower customer service expenses), as well as lower uncollectible expenses, which will benefit all customers. The Company believes that allowing deferral of its implementation and communication costs, without carrying costs, is reasonable for this program. Blue Granite believes that the Consumer Advocate’s position on this issue—to cap recovery of implementation costs and examine them in the next rate case—is a reasonable compromise position. The Company urges the

Commission to allow the Company to defer its implementation costs, capped at its estimate of \$50,000 as presented in this case, and subject to scrutiny before recovery through rates is authorized. (Tr. p. 764.25-26.)

### **Consumer Advocate Position**

The Consumer Advocate supports the Company's proposal for a Round-Up program, but recommends that a cap be placed on the deferral of costs relating to modifying the billing and customer service systems to accommodate the Round Up program. The Consumer Advocate further recommends that the deferred costs be subject to scrutiny in the Company's next rate case. (Tr. p. 651.21.)

### **ORS Position**

The ORS also supports the Round-Up program, but contends that Blue Granite's costs of implementing and communicating should be borne by shareholders. ORS therefore recommends that the pro forma adjustment for bill inserts and flyers be rejected, and recommends denial of the proposed deferral and recovery on the basis that Blue Granite's costs are not known and measurable, and do not contribute to the provision of safe and reliable water and sewer service. (Tr. p. 1190.14-15.)

### **Commission Findings**

The Company's proposed "Round Up" program will, through voluntary customer participation, assist low income customers with their water and wastewater bills. As noted by the Company, over time the program can produce lower disconnect/reconnect costs and lower uncollectible expenses. We find the Company's proposal to establish a voluntary "Round Up" program, in conjunction with the OEO and Community Action Agencies, is reasonable and we

approve the establishment of the program. Further, the fact that Commission approval is needed for this program indicates it is a Company service offering, notwithstanding the fact it is voluntary on the part of participating customers. The Round Up program has the potential to benefit all customers through lower disconnect/reconnect and uncollectible expenses. We therefore find that the pro forma adjustment for bill insert/flyers is reasonable and should be approved. Because we are approving this program, the Company must be made whole for the associated costs of implementation. Contrary to ORS's assertion, there is no requirement in the consideration of deferral requests that the costs be known or measurable; that is instead a requirement applicable to consideration for recovery in rates, which would occur in a future base rate filing in this situation. We approve the Company's proposal, as modified by the Consumer Advocate, to defer for recovery in its next base rate case its implementation costs associated with the program, up to a cap of the Company's estimate of \$50,000 for such costs.

**xi. Rate Case Expense and Other Legal Expenses**

As discussed below, we find that the remaining unamortized rate case expenses from Docket Nos. 2015-199-WS and Docket No. 2017-292-WS were appropriately deferred and are appropriately recovered in this proceeding

**Company Proposal**

Mr. DeStefano testified that the Company's regulatory expense has been adjusted for the total estimated cost of the filing of this case and the unamortized portion of the prior case and rehearing process, amortized over 3 years. (Tr. p. 763.11.)

**Consumer Advocate Position**

Consumer Advocate Witness Morgan proposed to exclude the remaining unamortized rate case and rehearing expense deferrals from the prior rate case.

### **ORS Position**

ORS Witness Sullivan proposed several proposed adjustments to outside services-other expenses, particularly legal expenses (see Adjustment Nos. 21c and 21e). ORS's proposed adjustments relate to: (1) removal and deferral of \$31,788 in legal costs related to a pending action; (2) removal of \$151,589 of legal costs related to Congaree Riverkeeper litigation, consistent with the Commission's Rehearing Order in Docket No. 2017-292-WS, which is currently open to appeal; (3) addition of \$168,310 related to activity from the I-20 condemnation; and (4) removal of \$36,864 from Test Year activity related to regulatory proceedings that will be combined with the deferred rate case expenses from this current proceeding.

### **Company Response**

Mr. DeStefano testified in rebuttal that the Company is in agreement with many of Mr. Sullivan's proposed adjustments to legal expenses. Specifically, the Company agrees to: (1) remove and defer \$31,788 in legal costs related to a pending action; (2) remove \$151,589 of legal costs related to Congaree Riverkeeper litigation, consistent with the Commission's Rehearing Order in Docket 2017-292-WS, which is currently open to appeal; (3) add \$168,310 related to activity from the I-20 condemnation; and (4) remove \$36,864 from Test Year activity related to regulatory proceedings that will be combined with the deferred rate case expenses from the current proceeding. (Tr. p. 764.30-31.)

However, Mr. DeStefano testified that the Company disagrees with the removal of \$7,143 in legal expenses related to services prior to the Test Year, without also reviewing post-Test Year

legal expenses for activity related to the Test Year period. Mr. DeStefano stated that the Company has identified \$7,203 in general legal expenses paid in the post-Test Year, that should be included for recovery if ORS's adjustment is accepted. Similarly, the Company has identified an additional \$16,132 in post-Test Year costs related to Docket Nos. 2018-358-WS and 2018-361-WS and recommends this amount be combined with the same activity identified in Adjustment No. 21c as Rate Case Expense for the current proceeding. Mr. DeStefano supported both the \$7,203 and \$16,132 figures noted above with his Rebuttal Exhibit No. 2. (Tr. p. 764.31.)

Mr. DeStefano added that the Company does not disagree with the rate case expense proposed by the ORS, which incorporates costs supported through the audit cut-of date. He noted that this amount is subject to change as the Company provides additional documentation for costs incurred during the pendency of this proceeding. (Tr. p. 764.31.)

With respect to the Consumer Advocate's proposed exclusions, Mr. DeStefano testified that Witness Morgan erroneously excluded remaining unamortized rate case deferrals from Docket 2015-199-WS, which are included in both the Company's and ORS's figures. Additionally, Mr. DeStefano noted, the Company and ORS have included the rehearing costs, as that proceeding was initiated by ORS's Request for Reconsideration after Order 2018-345 was issued in Docket 2017-292-WS. Despite the Consumer Advocate's assertion that it was "limited to a few issues," Mr. DeStefano testified that these issues were complex and required the preparation of direct and rebuttal testimony, a merits hearing, the preparation of a proposed order, and other matters requiring the incurrence of rate case expenses, none of which the Consumer Advocate challenges as being unreasonable. (Tr. p. 764.32.)

### **Commission Findings**



We agree with Blue Granite and the ORS that the remaining unamortized rate case deferrals from Docket No. 2015-199-WS, and the rehearing costs associated with Docket No. 2017-292-WS, were appropriately deferred and are appropriately recovered as rate case expense in this proceeding. We understand that these are rate case expenses and involved complex issues. We find that the Company's proposal for recovery of these expenses, with which the ORS agrees, should be authorized.

The Company is authorized to include rate case expenses incurred in this rate case through the date of the last public night hearing, March 5, 2020. After the hearing, the Company presented documentation supporting total rate case expenses of \$873,542, to be amortized over a three-year period, or \$291,181 annually. Because the additional rate case expenses are known and measurable, the Commission will allow them to be included in the total rate case expense and amortized over three years. This amount amortized over three years less the Company's per book amount yields a post-hearing adjustment of \$182,886.

#### **xii. Rent Expense**

As discussed below, we find that the evidence in the record supports Blue Granite's proposed rent expense adjustment to account for employees allocated to the Company but who are physically located in Charlotte.

#### **Company's Position**

In its application, the Company adjusted rent expense to reflect pro forma annualized effective leases. (Tr. p. 763.13.) Witness DeStefano explained the Company's disagreement with ORS's proposed pro-forma rent expense. Mr. DeStefano testified that there are workspaces assigned to ten employees in the Greenville office, and two employees have job duties that allocate

their time across the Atlantic region. (Tr. p. 764.32.) However, other Atlantic region employees provide support for the Company who are not primarily located in Greenville, and the Company did not initially request allocations of the Charlotte regional office costs for other Atlantic region and Shared Services employees that support the Company; the cost of those customers to serve the Company's customers is \$18,568. (Tr. p. 764.32.) Therefore, should the Commission accept ORS's proposed rent expense adjustment of (\$11,019), that adjustment should be further modified by an increase of \$18,568 to account for employees serving the Company's customers from Charlotte. (Tr. p. 764.33.) The Company supported this adjustment modification with DeStefano Rebuttal Exhibit No. 3, which provided the underlying calculations.

#### **ORS's Position**

ORS proposed an adjustment in the amount of \$84,839 to rent expense for pro forma annualized leases, a decrease of \$10,987 from the Company's proposed adjustment of \$95,826. (Tr. p. 1115.13.) Mr. Sullivan explained the variance is attributable mainly to ORS's proposal to decrease the Greenville office annual lease expense to correctly allocate lease expense for two employees assigned to the Atlantic Division based on the Company's response to Audit Request #17 which stated only 34.94% of their duties are applicable to the Company. (Tr. p. 1115.13.)

In surrebuttal, Mr. Sullivan disagreed with the Company's proposal to increase rent expense for employees of the Charlotte office because the Company did not include these amounts in its application. (Tr. p. 1116.2.) As such, ORS claims it was unable to audit the claimed expenses. (Tr. p. 1116.3.)

#### **Commission Finding**

ORS correctly pointed out that the Company initially sought to include in its rent expense certain employees who work in the Greenville office but whose duties are not fully assigned to solely the Company but rather to the larger Atlantic division. It is therefore appropriate to adjust the proposed rent expense by (\$10,987). However, the evidence also demonstrated that other Atlantic division employees provide support for the Company who are not primarily located in Greenville, and the cost of those employees to serve the Company's customers is \$18,568. (Tr. p. 764.32). Therefore, because Commission accepted ORS's Rent Expense adjustment, the Commission believes it is reasonable and equitable—and the record evidence supports—an increase to the rent expense adjustment of \$18,568 to account for employees serving the Company's customers from Charlotte, resulting in a net rent expense adjustment of \$7,581.

### **xiii. Insurance Expense**

As discussed below, we accept ORS's adjustment based on actual insurance expenses and find that the Consumer Advocate's concern is therefore moot.

#### **Company's Position**

Insurance expense was adjusted based on estimated policy premiums and deductible costs as of time of filing. The Company has since provided updates for the policy premiums determined upon renewal. (Tr. p. 763.13.) In its rebuttal, the Company agreed to ORS's position, which updates as-filed estimates for policy premiums confirmed in the Company's insurance renewal process, completed and effective November 1, 2019. (Tr. p. 764.33.) As such, the Consumer Advocate's concern about using estimates is moot. (Tr. p. 764.33.)

#### **ORS's Position**

ORS proposed an adjustment of \$163,371 to insurance to reflect the most recent insurance policy premiums and deductible expenses. (Tr. p. 1115.13.) Mr. Sullivan stated that the Company's proposed adjustment of \$201,243 to per book insurance expense based on policy premiums and deductible expenses as of the filing of the application. (Tr. p. 1115.13.) ORS's proposal is based on updates the Company provided to Audit Request #11, as of November 15, 2019, and ORS proposes to use the level of actual known and measurable 2019 deductibles in the calculation of the ORS adjustment. (Tr. p. 1115.13, 1115.14.)

#### **Consumer Advocate's Position**

Consumer Advocate Witness Morgan asserts that it is appropriate to reflect only the actual known insurance premiums rather than estimates. He recommended an adjustment to O&M expense to remove the estimated expense presented by the Company. (Tr. p. 651.17, 651.18.)

#### **Commission Finding**

The Commission initially notes that Blue Granite and ORS are in agreement that insurance policy premiums and deductibles, updated as of November 1, 2019, are the appropriate data points to use as opposed to estimates. We agree that the use of actual insurance expenses, which are known and measurable figures, is preferable to using estimated amounts. *See* Order No. 2004-434 at 16, Docket No. 2004-90-WS (Sept. 17, 2004) ("Using actual premium amounts is preferable to using estimated amounts."). We also note that this determination causes the Consumer Advocate's concern to become moot. We therefore find ORS's adjustment of \$163,371 is appropriate.

#### **xiv. Administrative Office Upfit Costs**

As discussed below, the evidence supports the conclusion that the Company made a reasonable business decision to relocate its headquarters office, and that the associated upfit costs

were necessary and reasonable. Additionally, while ORS gave testimony that, in its opinion, the office upfit costs should be disallowed, it offered no evidence that would overcome the presumption—in addition to the evidence offered by the Company—that the business decision to relocate and the resulting office upfit costs were reasonable. We therefore reject ORS’s proposal to exclude the office upfit costs from the Company’s revenue requirement.

### **Company Proposal**

The Company’s proposed rates reflect costs associated with upfitting its new headquarters office.

### **ORS Position**

ORS Witness Maurer proposed to disallow the Greenville office upfit costs in their entirety on the grounds that the decision to relocate the headquarters office from Columbia to Greenville was unreasonable. (Tr. p. 1201.7-13.) Witness Maurer asserts that the relocation of the Company’s office was part of its rebranding effort. (Tr. p. 1202.8.)

### **Company Response**

The Company disagrees with the ORS’s proposed exclusion of the Greenville office upfit costs. In his rebuttal testimony, Company Witness Denton addressed both the reasonableness of the business decision to relocate its headquarters office, as well as the reasonableness of the upfit costs themselves. With regard to the relocation decision, Mr. Denton stated that the Company’s Columbia office was located in an industrial park with no other office buildings and no amenities, like restaurants, nearby. He stated that the former location was not viable for attracting and retaining talented employees. Accordingly, the Company made the decision to relocate its headquarters office. Mr. Denton noted that this decision was consistent with and important to the

Company's long-term strategic plan to improve performance and service to customers. He noted this business decision to relocate to Greenville was supported by labor data and statistics indicating that the attributes of Greenville versus Columbia/West Columbia better match the Company's long-term goals of attracting and retaining talented employees. Mr. Denton noted that the Company and the industry as a whole are facing aging workforce issues, and the eligible workforce is shrinking, so ensuring that the right professionals are being attracted to the Company and retained by the Company is fundamental to the Company's ability to continue providing quality and cost-effective service. He emphasized that the labor data and statistics relied on by the Company indicate that Greenville has a larger workforce and a larger expected population growth than Columbia and West Columbia. He stated that the Company believes that these demographics will help it in adding new employees. Additionally, he stated that the Greenville office is located close to the Company's outside engineering company and peer utilities. Finally, he noted that since the relocation to Greenville, the Company has been able to successfully attract several strategic new hires. (Tr. p. 355.4-8.)

With regard to the reasonableness of the upfit costs themselves, Mr. Denton emphasized the necessity of having a headquarters office, and once the decision to relocate was made, the necessity of incurring upfit costs whether it relocated within Columbia/West Columbia, to Greenville, or somewhere else. Mr. Denton also testified that virtually all of the costs were necessary to making the office space ready for work. These costs included putting up drywall, installing electrical and telecommunications lines, painting, purchasing desks, all the things necessary to work in an office space. He stated that the offices are up to date and functional, but they are not luxurious or gold-plated. He stated that a functional headquarters office space is

necessary for employees to provide utility service, and the associated costs should be reflected in rates. He provided cost benchmarking data indicating that on a per square foot basis, the Greenville upfit costs were below average when compared to other areas included in the benchmarking study. He also noted that the size of the Greenville office is reasonable; it houses 10 employees in 4,287 square feet, while the previous office housed 7 employees in 4,050 square feet. (Tr. p. 355.4-8.) It was also revealed at the hearing that Blue Granite had been able to make a number of new hires since its relocation of employees who appear to be well-qualified. (Tr. p. 472, line 9 through p. 473, line 8; Hearing Ex. No. 12.)

### **Commission Findings**

The evidence indicates that the Company made a reasonable business decision to relocate its headquarters office to Greenville. Although the Commission hesitates to second-guess management business decisions such as this, we note that the Company supported the reasonableness of its decision with evidence about labor growth and availability, as well as convenience of the location vis-à-vis its outside engineering company and certain peer utilities. Additionally, the evidence indicates that the upfit costs themselves were reasonable. The Company demonstrated that the square footage is lower, the number of employees housed in the new office is greater, and the overall costs are below average per a benchmarking study.

Further, while ORS gave testimony that, in its opinion, the office upfit costs should be disallowed, it offered no evidence that would overcome the presumption—in addition to the evidence offered by the Company—that the business decision to relocate and the resulting office upfit costs were reasonable. *See Hamm v. S.C. Pub. Serv. Comm’n*, 309 S.C. 282, 286, 422 S.E. 110, 112 (1992); *Utils. Servs. of S.C., Inc. v. S.C. Office of Regulatory Staff*, 392 S.C. 96, 110, 708

S.E.2d 755, 762-63 (2011). The mere assertion by ORS that the upfit costs should be disallowed is insufficient to support its recommended disallowance. *See Young v. Tide Craft, Inc.*, 270 S.C. 453, 242 S.E.2d 671, 678 (1978) (finding that opinions are of no probative value without an evidentiary showing of the facts upon which the opinion is predicated); *Parker v. S.C. Pub. Serv. Comm'n*, 281 S.C. 215, 314 S.E.2d 597 (1984), modified, 288 S.C. 304, 342 S.E.2d 403 (1986) (finding same); *Hickman v. Aetna Life Ins. Co. of Hartford*, 166 S.C. 316, 164 S.E. 878 (S.C. 1932) (finding that a mere assertion or expression of opinion cannot create an issue of fact). Further, while ORS attempts to link the Company's relocation with its rebranding effort, the evidence does not support such a connection. Blue Granite's decision to relocate was strategic in light of relevant labor market data and the record evidence supports the conclusion that the relocation did, in fact, result in the hiring of well-qualified new employees.

Consistent with the above, we reject ORS's proposal to exclude the office upfit costs from the Company's revenue requirement.

**xv. Employee Service Award Costs**

As discussed below, we accept Blue Granite's inclusion of these nominal amounts for employee service awards, which represent a small part of the overall compensation package for the Company's employees.

**Company Proposal**

In its proposed revenue requirements, the Company included nominal amounts related to employee service awards.

**ORS Position**



ORS Witness Jackson recommended removal of the costs associated with the employee service awards (see Adjustment No. 17B). (Tr. p. 1133.6-7.)

### **Company Response**

In rebuttal, Mr. Denton reiterated that Blue Granite is engaged in a long-term effort to substantially improve its performance. He stated that, as part of that effort, Blue Granite is working to attract and retain well-qualified employees who are dedicated to the Company's mission of improving its performance. He testified that running a utility is a complicated endeavor that requires talented and experienced employees, and the employee service awards at issue are a component of the Company's overall compensation package offered to its employees. Further, he testified the awards referenced by ORS are consistent with the Company's market-competitive compensation package, and the awards program supports the Company's efforts to successfully attract and retain well-qualified employees. He opined that the \$3,211 in employee awards was prudently incurred. (Tr. p. 354.8-9.)

### **Commission Findings**

There is no evidence that Blue Granite's employee compensation as a whole is above-market or excessive. The evidence indicates, instead, that these nominal amounts for employee service awards are a small part of the overall compensation package for the Company's employees, and are consistent with the Company's goal of attracting and retaining talented employees. Accordingly, we reject the ORS's proposed exclusion of these amounts from revenue requirements, and we find that the service award amounts are reasonable.

**xvi. LETTS Tank Pumping Charges**

As discussed below, we approve the proposal contained in ORS Witness Bickley's surrebuttal testimony related to LETTS tank pumping charges, which includes language authorizing the Company to take immediate actions to pump a LETTS tank under a scenario which presented a health risk to the environment, public or customer.

**Company's Position**

In Paragraph 24 of its Application, the Company seeks authority to amend its tariff language and fees related to Solid Interceptor ("LETTS") Tanks. The Company proposes to change the Pumping Charge from \$150 to the actual cost to access, pump, and service the tanks on a periodic basis. This change is necessary to permit the Company to recover from the responsible customer the actual costs associated with the necessary task of pumping and cleaning a customer's tank when excessive solids have accumulated in the interceptor tank. The actual cost of performing this task, inclusive of the cost to access the tank, is often more than the currently effective charge of \$150 and needs to be performed every three to five years. The Company therefore proposes to bill the applicable customer for the actual cost of pumping and cleaning the tank, and that the pumping charge be included as a separate line item on the customer's next bill. The Company would allow, should the customer desire, to bill the customer's pumping charge in twelve equal monthly installments. (Tr. p. 362.13.)

In response to ORS's position, Mr. Mendenhall stated his concern that allowing customers to seek alternative service providers could lead to sanitary sewer overflows. (Tr. p. 363.11). When an interceptor or LETTS tanks is full, it requires prompt response, and ORS's proposal prevents

the Company or its on-call providers from acting immediately to pump an interceptor tank. (Tr. p. 363.11, 363.12.)

During cross-examination, Mr. Mendenhall stated the Company was close to an agreement with ORS in order to allow customers to seek out its own vendor to clean LETTS Tanks during non-emergency situations. (Tr. p. 364.) He testified that ORS's proposal remained subjective regarding the definition of an "emergency situation" that would justify the Company pumping the tank. (Tr. p. 395.)

### **ORS's Position**

Mr. Bickley stated that the Company provided thirty instances of pumping charges during the Test Year, and the pumping work was generally completed by three different third-party vendors. (Tr. p. 1190.4.) ORS determined an average cost to preform pumping of a LETTS Tank was approximately \$750 during the Test Year. (Tr. p. 1190.4.) Mr. Bickley stated that under the proposed tariff language, a Blue Granite customer with a LETTS Tank does not have the option of obtaining quotes from the Company or another qualified third-party vendor or contractor. (Tr. p. 1190.4, 1190.5.) ORS's position is that Blue Granite customers should be allowed to choose to have pumping services performed by a third-party vendor, at the customer's expense. (Tr. p. 1190.6.) In order to facilitate this choice, the Company should be required to provide an estimate of the actual cost of the pumping service to the customer. (Tr. p. 1190.7.) Should the customer authorize the Company to perform the service, the Pumping Charge should not exceed the estimate, and be billed to the customer as a separate line item in the next bill, or in twelve equal monthly installments. (Tr. p. 1190.7, 1190.8.)

In surrebuttal testimony, Mr. Bickley modified ORS's proposal by adding language authorizing the Company to take immediate actions to pump a LETTS Tank under a scenario which presented a health risk to the environment, public or customer. (Tr. p. 1191.3.) He also suggested modified language related to third-party vendors following laws and regulations. (Tr. p. 1191.3, 1191.4.)

### **Commission Finding**

The record demonstrates that the Company has agreed in large part with ORS's position. Specifically, the Company appears to have consented to providing the customer with the opportunity to seek out their own vendors to clean a LETTS Tank. In the circumstance of a non-emergency situation, the Company would provide an estimate of the actual cost of the pumping service for that customer, and the customer would then have the opportunity to either authorize the Company to perform the service at the estimated cost, or allow the customer to use another qualified third-party vendor or contractor to perform the service. We find these procedures balance the public health's interest in inspecting and pumping LETTS Tanks with the customer's interest in having the opportunity to seek such service from a qualified contractor or vendor.

The Company expressed a concern with allowing the above process in an emergency situation, due to the length of time it could take for a customer to obtain a Company estimate, seek alternative service providers, deliberate on their choice, and only then schedule and obtain pumping service. The ORS indicated they agreed with this approach. We agree with the Company's concern that this process could lead to sanitary sewer overflows, as the evidence and natural reason indicate that a full LETTS Tank requires a prompt response to prevent an overflow into the environment. We therefore approve the language proposed in ORS Witness Bickley's

surrebuttal testimony, which includes language authorizing the Company to take immediate actions to pump a LETTS Tank under a scenario which presented a health risk to the environment, public or customer.

**xvii. Cost of Service and Tariff Rate Design**

As discussed below, contrary to the Consumer Advocate's position, we believe that it would be premature to order changes to Blue Granite's rate designs based on an incomplete record, *i.e.*, without a cost of service study. We find and direct that Blue Granite should prepare and present a cost of service study in its next rate case, and we approve and authorize the Company to defer for subsequent recovery the costs associated with the preparation and presentation of such cost of service study, and to accrue carrying costs at the Company's cost of debt until recovery.

**Company Proposal**

The Company did not propose further rate consolidation in this case, and proposes to maintain its existing rate design structure for rates approved in this proceeding – that is, to continue use of 1) Water Service Territories 1 and 2, with segregation of Supply Only and Distribution Only customers based on purchased water supply by third-party vendors, and 2) Consolidated Sewer Service Territory, with segregation of Collection & Treatment Only and Collection Only customers based on purchased sewer treatment from third-party vendors. The Company proposed to split the volumetric charge for Distribution Only customers into a Distribution Charge and a Purchased Water Charge, the latter of which would explicitly recover purchased water supplier costs for the respective consolidated service territory. The Company also proposed a similar split for sewer Collection Only customer charges, shown as a Collection Charge and Treatment Charge,

the latter of which would explicitly recover purchased sewer treatment supplier costs for the consolidated sewer service territory.

### **Consumer Advocate Position**

Consumer Advocate Witness Mierzwa testified as follows with respect to rate design:

- Blue Granite’s existing base facility/monthly customer charges should remain unchanged, and any revenue increases should be recovered through increases in volumetric usage charges. He stated that a cost of service study would show that the Company’s base charges are too high, and that they should be approximately \$10.00, as opposed to the Company’s proposed \$22.09 and \$38.58 for Water Service Territories 1 and 2, respectively.
- In rebuttal, Blue Granite should address whether it would be reasonable to assess volumetric charges for sewer service based on customer water service usage, which is a common practice and which may better match cost causation and cost recovery.
- In rebuttal, Blue Granite should also address whether its current system of assessing commercial customers sewer service charges based on each customer’s Single-Family Equivalent (“SFE”) is reasonable; SFE-based rate design may not provide for a reasonable matching of cost causation and recovery.

(Tr. p. 633.3-9.)

### **ORS Position**

ORS Witness Sandonato recommends a gradual further consolidation of the Company’s Service Territory 1 and Service Territory 2 water rates, by allocating the revenue requirement in this case “in a more equitable manner” – specifically, by limiting the revenue requirement increase for Service Territory 2 to no more than 31% of the total water service revenue requirement. He

also suggested that the Company should present a cost of service study in its next rate case. (Tr. 1213.13-15.) Mr. Sandonato also recommends no segregation of charges, as proposed by the Company, for Distribution Only and Collection Only customers, but instead to maintain the current charge structures for these customer groups. (Tr. 1213.16.)

### **Company Response**

Mr. DeStefano testified in rebuttal that the Company agrees with the ORS that continued rate consolidation is in the long-term best interest of its customers. Further, he testified that, as suggested by ORS, the Company is agreeable to filing a cost of service study in its next rate case, which would best delineate the cost drivers and provide the best roadmap to consolidating rates and setting appropriate base facility and volumetric charge levels for the Company's customer groups. He added that, should the Commission direct Blue Granite to preparing a Cost of Service Study before its next rate case, Blue Granite requests that the Commission approve such and authorize the deferral of the associated costs along with its other rate case filing and processing expenses. (Tr. p. 764.36-39.)

With regard to Consumer Advocate Witness Mierzwa's recommendations for the Company's water base facility charges, Mr. DeStefano disagreed. He stated that Witness Mierzwa's analysis using the base-extra capacity method to determine an appropriate Base Facility Charge is incomplete, as it does not account for post-Test Year plant additions, updated depreciation rates, allocations of cash working capital, and other pro forma adjustments incorporated into the Consumer Advocate's proposed revenue requirement. In addition, he stated that a comprehensive cost of service study would incorporate cost allocations between service territories and water and sewer on a more detailed level. As such, he testified that the Company

believes it is premature to draw conclusions about the appropriate Base Facility Charges based on the data available in the current proceeding. Rather, the Company recommends, in agreement with ORS witness Sandonato, that a cost of service study be filed in the next rate case to adequately support further adjustments to rate structure and revenue requirement consolidation. (Tr. p. 764.39-41.)

Mr. DeStefano also addressed Blue Granite's current system of assessing commercial customers' sewer service charges based on each customer's single-family equivalent ("SFE"). Mr. DeStefano testified that the Company believes it is most prudent to provide a cost of service study in its next base rate filing to support the potential for such changes in its rate structure.

With respect to the reasonableness of the Company assessing volumetric charges for sewer service based on customer water service usage, Mr. DeStefano noted that there are several considerations to implementing a volumetric component to sewer rates in the Company's service territories. First, he stated, only approximately half the Company's sewer customers are also provided water service by the Company, and thus the lack of water meter read data prevents Blue Granite from providing volumetric billing to the sewer-only customers. Additionally, he testified that the Company does not believe an unadjusted use of metered water usage is a reasonable proxy for sewer flows. He observed this is especially true in seasonal periods, where customers are using irrigation systems, filling pools, and otherwise increasing the proportion of water use that does not flow through the Company's sewer collection system. Finally, Mr. DeStefano noted that there are several ways to structure sewer volumetric rates (*i.e.*, winter averaging, usage caps), and a detailed analysis of the Company's customer data in future proceedings can be completed to further explore such a proposal. (Tr. p. 764.39-41.)



**Commission Findings**

We agree with the Company that it would be premature to order changes to Blue Granite's rate designs based on an incomplete record and evidentiary support, *i.e.*, without a full cost of service study. All parties appear to agree that Blue Granite should present a cost of service study in its next rate case. Accordingly, we find and direct that Blue Granite should prepare and present a cost of service study in its next rate case. Further, we approve and authorize the Company to defer the costs associated with the preparation and presentation of such cost of service study, to be considered for recovery along with rate case filing expenses incurred in the next base case. We also approve the Company's proposed segregation of purchased water and sewer treatment expense recovery for Distribution Only and Collection Only customers, as such segregation will allow great transparency into the cost drivers affecting the tariff rates and resulting customer bills. Finally, while we do not order further rate consolidation in this case, we encourage Blue Granite to continue to pursue rate consolidation in future rate cases.

**xviii. Other Issues****I-20 Condemnation Proceeds**

In response to Commissioner questioning and on redirect, the Company provided testimony that the I-20 system was removed from rate base in the last rate case; that the Company had an acquisition adjustment still on its books from the acquisition of Blue Granite's parent by Corix; that shareholders bore the risk of loss on that amount and the Company's stranded investment in the system; and that the ultimate gain was recorded "below the line", consistent with the Uniform System of Accounts (Tr. p. 985-986). Components of this testimony, including that the system was entirely removed from rate base, was confirmed by ORS Witness Sullivan, who

also confirmed that the Company's accounting treatment related to the system was appropriate. (Tr. p. 1142-1145.)

Consistent with this Commission's precedent, and with the principle that the "right to gain follows the risk of loss," we believe that the Company's accounting treatment associated with the I-20 condemnation was appropriate. Per our precedent, and consistent with reasoned judgment, when the utility, rather than ratepayers, bear the risk of loss on an asset, any gain that may instead result inures to the benefit of the utility. The Commission was faced with this exact situation in the 1980s as related to the Catawba nuclear facilities owned by Duke Power Company. The utility recorded the sale of the facilities on its books to Account 421.1, a nonoperating account, as "below-the-line" income. As explained in the Commission's order, this recording "is consistent with the Uniform System of Accounts which would preclude a charge against operating income has the sale of facilities resulted in a loss, thereby insulating the interests of the Company's ratepayers against the possibility of a loss." Order No. 80-474 at 33, Docket No. 79-300-E (Aug. 29, 1980). As discussed in a follow-on order, that treatment was unsuccessfully appealed to the Circuit Court and not pursued further even though other issues in that proceeding were further appealed to the S.C. Supreme Court. Order No. 85-1001 at 4, Docket No. 85-78-E (Nov. 7, 1985). As noted in that order, "[t]he purpose of not flowing the 1978 gain to the ratepayer in Order No. 80-474 was to insulate the ratepayer from a loss which could have occurred from a sale rather gain." That is precisely the situation in this case. The I-20 system was removed from rate base, the Company's shareholders risked a loss in litigation based on the liabilities remaining below-the-line on the Company's books, and it so happened that the Company was successful in obtaining a net gain on

the transfer of the system assets. We therefore find that the Company's accounting treatment was appropriate.

**Clearwater Solutions Contract**

Mr. DeStefano testified that the Company entered into a contract operator agreement with Clearwater Solutions after the end of the Test Year. In the case, the Company proposed adjustments to the Test Year balances for various expense accounts to reflect the Clearwater Solutions contract – both the addition of contract operator costs and the removal of associated Company labor, etc., that is superseded by the Clearwater Solutions contract. Mr. DeStefano noted that these adjustments net to a savings for customers in the current rate case. (Tr. p. 763.13, 763.18.)

At the hearing, counsel for the Town of Irmo suggested that customers were being asked to pay for O&M costs twice, that Clearwater Solutions somehow constituted an unregulated utility, and he implied that there might be an affiliated ownership interest between Blue Granite and its contractor, Clearwater Solutions. (*E.g.*, see Transcript at pp. 373-375; 479-484; 773-778; 858-870.)

During cross-examination, Mr. DeStefano made clear that, to the extent maintenance may not have been performed in previous years, customers would not have paid for such maintenance, because rates are set based upon actual, historical costs incurred by the utility (Tr. p. 868-870). In addition, during cross-examination, Mr. Mendenhall emphasized that Clearwater Solutions is but a contractor of Blue Granite's, and Blue Granite is responsible for overseeing its contractor and remains the utility regulated by this Commission. (Tr. p. 374.) Finally, Mr. Mendenhall confirmed

that there is no affiliate interest relationship between Blue Granite and its contractor, Clearwater Solutions. (Tr. p. 457.)

The evidence does not demonstrate that customers “paid twice” for maintenance expenses, nor does the evidence indicate any affiliate interest relationship between Blue Granite and its contractor, Clearwater Solutions. Further, the Commission is well aware that utilities retain contractors to assist them in the provision of utility services to customers. These contractors are not utilities; rather, the Company oversees the contractor’s work and remains the regulated entity subject to the Commission’s jurisdiction. We would also remind parties that the tools of discovery are continually available to the extent a party seeks information germane to the proceeding.

Finally, as related to S.C. Code Ann. Reg. 103-541—while the Clearwater Solutions contract relates to the provision of service by the Company to its customers—there is no evidence and there has been no suggestion that the contract has impacted, impaired, or pertains to Blue Granite’s “fitness, willingness, or ability” to provide service. Broadening our interpretation of that regulation to require pre-approval of any contract that pertained to the provision of water or sewerage service would unduly restrict utilities’ ability to conduct business and would be inconsistent with our intent in promulgating the regulation, which was instead to monitor the ability of utilities to provide service.

### **Elevated Storage Tank Property**

Consumer Advocate Witness Morgan proposes to remove \$350,000 from rate base associated with the purchase of land to facilitate an elevated storage tank that was not complete in time to be eligible for inclusion in rates. (Tr. p. 658.11.) However, we note that the Company

removed this amount from rate base in its Direct Testimony, and such removal is reflected in ORS Adjustment No. 37. (Tr. p. 763.14, 1128.13.)

### **Hydrotank Expenses**

Consumer Advocate Witness Morgan also recommends an adjustment to rate base of \$73,000 to remove certain hydro tank-related expenses because they were incurred after the Test Year. However, the inclusion of such expenses recognizes that known and measurable changes occurring after the end of the Test Year should be reflected in rate base. *See Southern Bell Tel. & Tel. Co. v. Pub. Serv. Comm'n*, 270 S.C. 590, 602, 244 S.E.2d 278, 284 (1978) (“[W]e believe that the Commission should make any adjustments for known and measurable changes in expenses, revenues and investments occurring after the test year, in order that the resulting rates will reflect the actual rate base, net operating income, and cost of capital.”).

### **Pro Forma Plant Additions**

Consumer Advocate Witness Morgan proposed exclusion of the Company’s pro forma plant additions because the additions were scheduled to be placed in service after the end of the Test Year. (Tr. p. 651.12.) In his rebuttal testimony, Mr. DeStefano stated that the Company supplied multiple updates for actual plant activity post-Test Year, and such asset additions were confirmed to be in-service and benefitting customers during the ORS site visits in early January. For these reasons, Mr. DeStefano recommended that the Commission reject Witness Morgan’s proposed exclusions. (Tr. p. 764.41.)

The evidence demonstrates that the pro forma plant additions the Consumer Advocate proposes to exclude were in fact in-service and providing service to customers prior to the evidentiary hearings in this case, and that the associated costs were known and measurable and

therefore appropriately accounted for in this case. Accordingly, we find that such plant additions should be reflected in revenue requirements and rates in this case.

### **Return of EDIT Balance**

Consumer Advocate Witness Morgan also proposes that the EDIT balance should be used to offset deferred purchased water and wastewater treatment deferred costs. (Tr. p. 651.15.) The Company proposed to return the EDIT balance to customers through a one-time credit on bills. (Tr. p. 763.10.) We find that these proposals are functionally equivalent, while the Company's proposal will be simpler to implement and more easily verifiable, as well as provide customers the benefit of the return of these funds more promptly; we therefore approve the Company's proposal, as adjusted by ORS.

### **xix. Use of Charlotte Interconnection**

As discussed below, we deny York County's request to opine, in this base rate proceeding, on the requirements contained in its franchise agreement with the Company related to the Charlotte water connection.

### **York County's Position**

York County states that the Company's connection with the City of Charlotte is only for the provision of emergency water service. (Tr. p. 1029.6.) York County asks the Commission to find that the Company's use of the Charlotte water connection in the absence of the declaration of an emergency violates the Company's franchise agreement with York County. (Tr. p. 1029.6.)

### **Blue Granite's Position**

Blue Granite states that this rate case relates exclusively to Blue Granite's need for a rate adjustment, has no bearing on the legal interpretation of the franchise agreement, and therefore

this is an inappropriate context for the Commission to weigh in on this issue. (Tr. p. 355.9.) Blue Granite also states that, while the franchise agreement required the installation of the Charlotte water connection, it does not limit the Company's use of the connection only to times of emergency. (Tr. p. 355.9.) Blue Granite points out that the Charlotte water connection provides water at a rate of \$3.76/1,000 gallons, compared to York County's rate of \$4.42/1,000 gallons. (Tr. p. 355.10.) Therefore, the more the Company uses the Charlotte water connection, the lower the costs will be to Blue Granite's customers. (Tr. p. 355.10.)

### **Commission's Finding**

We find that this rate case is not the appropriate context for consideration of this issue. Pursuant to S.C. Code Ann. § 58-5-240, this proceeding relates exclusively to the consideration of Blue Granite's filed rates and charges, not the construction of its franchise agreements. Further, were even this Commission inclined to provide an opinion on this issue, it is not vested with the authority to resolve what is essentially a breach of contract claim articulated by York County. *See* Order No. 1999-888, Docket No. 1999-339-E (Dec. 20, 1999) (providing a legal exegesis as to the Commission's lack of authority to resolve breach of contract claims). As a creature of statute, this Commission possesses "only those powers expressly conferred or necessarily implied for it to effectively fulfill the duties with which it is charged." *Captain's Quarters Motor Inn, Inc. v. S.C. Coastal Council*, 306 S.C. 488, 490, 413 S.E.2d 13, 14 (1991). We have not been conferred with the power to adjudicate breach of contract claims.

Finally, were this base rate proceeding the appropriate context for considering this breach of contract claim, and were this Commission statutorily empowered to adjudicate this breach of contract claim, we would find that the franchise agreement does not—by its plain terms—bear on

under what circumstances the Company must or may use the Charlotte water connection. We also find helpful the fact that the more Blue Granite uses the Charlotte water connection, the less its customers pay for water. *See* Order No. 2019-567 at 2, Docket No. 2019-223-W (Aug. 14, 2019) (“[T]he rate impact of purchased water will be evaluated by the Commission at the next rate case, and . . . ORS and other parties may address utilization of least-cost supply in any purchase water recovery sought by the Company.”). In light of all of these factors, we deny the relief requested by York County.

## VI. FINDINGS OF FACT AND CONCLUSIONS OF LAW

1. We find and conclude that Mr. D’Ascendis’ recommended cost of equity of 10.25% for Blue Granite is reasonable and should be approved. This finding is supported not only by our analysis and findings concerning the ROE methodologies, inputs, and assumptions, but also by our view that the DCF method should be given relatively less weight, our view that the ECAPM method should be given consideration, our view that Blue Granite’s company-specific risks are relevant and support an ROE at the higher end of a reasonable range of ROEs, and evidence of the need for the Company to maintain financial integrity in light of its ongoing capital financing needs.

2. We find that Blue Granite’s overall cost of capital is 8.12%, that such is just and reasonable and supported by the reliable, probative, and substantial evidence on the whole record.

The cost of capital is computed as follows:

Description	Ratio	Cost	Weighted Cost
Common Equity	52.91%	10.25%	5.42%
Long Term Debt	47.09%	5.73%	2.70%
Total	100.00%		8.12%

3. We find that Mr. Spanos’ proposed service lives and net salvage estimates are the most reasonable and his recommended depreciation rates should be approved. We find and



conclude that Mr. Spanos' testimony and proffered evidence were highly credible given his expertise in the field, his depreciation studies and the rationales therefor, and his approach of combining mathematical calculations with the application of expert professional judgment and visual curve fitting techniques greatly support the credibility of his testimony over that of over parties.

4. We find that the Company should be required to conduct leak testing on the four systems for which leak testing is economic, and to contract with a third party to have a water audit conducted. We also find that Blue Granite should be permitted to recover its third party purchased water and sewer treatment expenses, except non-revenue water amounts over 20 percent for the four systems for which leak detection is economic, i.e., Peachtree Acres, I-20, Hidden Lakes, and Hill and Dale systems.

5. We find that the pass-through mechanism, with the modifications directed in this Order, is a reasonable method by which Blue Granite can be made whole for its necessary third-party purchased water and sewer treatment service expenses, and that it benefits customers by regularly and predictably adjusting rates based on periodic changes in third-party service providers' rates.

6. We find that the rate design applicable to the pass-through mechanism should reflect the consolidated rate design already approved by this Commission.

7. We approve the procedure for the Company's annual pass-through mechanism as described above in the body of this Order.

8. Because we are approving the pass-through mechanism in this proceeding, and because the mechanism will be conducted annually as described above, we find that the Company

should be permitted to recover the costs associated with the mechanism's annual notice and filing as part of base rates, and the Company should be authorized to defer, on an interim basis, its pass-through expenses incurred from its vendors, as necessary until such costs are recovered through the pass-through mechanism.

9. We find that the Company's deferred maintenance expenses related to hydrotank inspections should be reflected in rates, as they are a reasonable and necessary part of providing water utility service.

10. We find that the amortization period for the decommissioning of the Stonegate water treatment plant and Friarsgate wastewater treatment plant should be matched to the remaining lives of the actual retired assets.

11. We find that the deferral balances for hurricane costs, I-20 Phase 2, Stonegate decommissioning and net book value, Friarsgate decommissioning and net book value, and EDIT reserves should be calculated to 4/30/2020, because there are no known and measurable changes to the deferral balances that occur between the audit cut-off date and this date.

12. We find that accumulated depreciation and CIAC amortization balances should utilize the same cut-off date for inclusion in rate base as their related gross plant in-service and CIAC components.

13. We conclude that the Company's Storm Recovery Expense using a five-year average is a reasonable approach as such is more reflective of recent conditions.

14. We find that the Company's proposed Storm Reserve Fund is a reasonable method by which to address extreme storms costs, but that the fund should be reevaluated during the Company's next base rate proceeding. We find that, contrary to the Consumer Advocate's

assertion, the Storm Reserve Fund is distinct from and in addition to the Company's more routine storm recovery expenses.

15. We find that the Company's proposed Round Up program is reasonable, and that the Consumer Advocate's recommendation that the Company defer the related implementation costs, up to a cap of the Company's estimate of \$50,000 for such costs, is reasonable and should be approved. We also find that the Company's pro forma adjustment for bill insert and flyer costs related to the Round Up program should be approved.

16. We find that the remaining unamortized rate case expenses from Docket Nos. 2015-199-WS and Docket No. 2017-292-WS were appropriately deferred and are appropriately recovered in this proceeding.

17. We find that the evidence in the record supports Blue Granite's proposed rent expense adjustment to account for employees allocated to the Company but who are physically located in Charlotte.

18. We find that ORS's adjustment based on actual insurance expenses is appropriate, and therefore find that the Consumer Advocate's concern is moot.

19. We find that the Company made a reasonable business decision to relocate its headquarters office to Greenville, and that the associated upfit costs were reasonable. We also find that ORS offered no evidence that would overcome the presumption and the evidence offered by the Company that the business decision to relocate and the resulting office upfit costs were reasonable.

20. We find that Blue Granite's inclusion of nominal amounts for employee service awards are reasonable and should be recovered.

21. We find that the proposal contained in ORS Witness Bickley's surrebuttal testimony related to LETTS tank pumping charges is reasonable in that it balances customer choice with protection from risks to the environment, public or customer.

22. We find that it would be premature to order changes to Blue Granite's rate designs without a cost of service study. We find that Blue Granite should prepare and present a cost of service study in its next rate case.

23. We find and conclude that the I-20 system was removed from rate base, the Company's shareholders risked a loss in litigation based on the liabilities remaining below-the-line on the Company's books, and therefore find that the Company's accounting treatment for that system was appropriate.

24. We find that the evidence does not demonstrate that customers "paid twice" for maintenance expenses, nor that there is any affiliate interest relationship between Blue Granite and its contractor, Clearwater Solutions.

25. We find that the rate base adjustment to account for hydro tank-related expenses was due to known and measurable changes and is appropriately reflected in rate base.

26. We find that the Company's proposal to return the EDIT balance to customers through a one-time credit on bills is reasonable.

27. We find that it would be unlawful and inappropriate for this Commission to opine, in this base rate proceeding, on the requirements contained in the franchise agreement between York County and the Company related to the Charlotte water connection.

## **VII. ORDERING PARAGRAPHS**

IT IS THEREFORE ORDERED THAT:

1. The calculation of base rates conforming to the findings contained within this Order shall be established based on a return on equity of 10.25% and an overall weighted cost of capital of 8.12%.

2. The calculation of base rates shall further be based on the Company's proposed service lives and net salvage estimates as reflected in the Company's proposed depreciation rates.

3. Blue Granite shall conduct or have conducted leak testing on the Peachtree Acres, I-20, Hidden Lakes, and Hill and Dale systems, and is authorized to defer the associated costs into a regulatory asset account, along with carrying costs at the Company's cost of debt.

4. Blue Granite is authorized to recover its third party purchased water and sewer treatment expenses, except non-revenue water amounts over 20 percent for the Peachtree Acres, I-20, Hidden Lakes, and Hill and Dale systems.

5. Blue Granite shall contract with a third party to have a water audit conducted, and is authorized to defer the associated costs into a regulatory asset account, along with carrying costs at the Company's cost of debt.

6. Blue Granite is authorized to implement the pass-through proceeding subject to the modifications and mechanism procedures directed in this Order, including the provision of a pre-filing notice, the filing of an annual application on or before March 1<sup>st</sup> of each year, the filing of comments by interested parties on or before April 15<sup>th</sup> of each year, and a Commission decision on or before June 1<sup>st</sup> of each year.

7. Blue Granite's rates shall be adjusted to account for the costs associated with the pass-through mechanism's annual notice and filing.

8. The calculation of base rates shall include the Company's deferred maintenance expenses related to hydrotank inspections.

9. The amortization period for the decommissioning of the Stonegate water treatment plant and Friarsgate wastewater treatment plant shall match the remaining lives of the actual retired assets.

10. The deferral balances for hurricane costs, I-20 Phase 2, Stonegate decommissioning and net book value, Friarsgate decommissioning and net book value, and EDIT reserves shall be calculated to April 30, 2020.

11. We find that accumulated depreciation and CIAC amortization balances should utilize the same cut-off date for inclusion in rate base as their related gross plant in-service and CIAC components.

12. Calculation of base rates shall include the Company's Storm Recovery Expense using a five-year average.

13. Blue Granite shall be authorized to establish a Storm Reserve Fund as proposed. The fund shall be reevaluated during the Company's next base rate proceeding.

14. Blue Granite shall be authorized to establish a Round Up program as proposed, and the Company is authorized to defer in a regulatory asset account the related implementation costs, up to a cap of the Company's estimate of \$50,000 for such costs, and is authorized to accrue carrying costs at the Company's cost of debt; calculation of base rates shall also reflect Blue Granite's pro forma adjustment relating to the Round Up program.

15. Calculation of base rates shall include the remaining unamortized rate case expenses from Docket Nos. 2015-199-WS and Docket No. 2017-292-WS.

16. Calculation of base rates shall include and account for the Company's office upfit costs.

17. Calculation of base rates shall include and account for any and all other findings made in this Order not expressly addressed in this section, including (1) a rate base of \$75,599,471, (2) Total Operating Expenses of 27,972,323, and 3) Total Operating Revenues of \$34,020,898, as shown in Order Exhibit No. 2, which is attached hereto.

18. Blue Granite is authorized to modify its LETTS tank pumping tariff language to conform to that set forth in ORS Witness Bickley's surrebuttal testimony.

19. Blue Granite shall prepare and present a cost of service study in its next rate case.

20. Blue Granite shall return the EDIT balance to customers through a one-time credit on bills as proposed.

21. The Company must include notice of its newly revised rates and provisions substantially in the form of the notice attached to this Order as Order Exhibit No. 3 to be included as a bill insert at the time rates are made effective.

BY ORDER OF THE COMMISSION:

\_\_\_\_\_  
Comer H. "Randy" Randall, Chairman

ATTEST:

\_\_\_\_\_  
Jocelyn Boyd, Chief Clerk/Executive Director